Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of	)	
	)	
Developing a Unified Intercarrier Compensation Regime	)	CC Docket No. 01-92
	)	
	)	

REPLY COMMENTS

OF

THE RURAL ALLIANCE

July 20, 2005

**REPLY COMMENTS
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EXECUTIVE SUMMARY

A close relationship exists between the intercarrier compensation issues at stake in this proceeding and the overall issue of Universal Service. Any intercarrier compensation reform proposal must be evaluated in the context of how it will affect the maintenance and advancement of critical Universal Service goals, including that of providing broadband connectivity to rural areas.

Rural carriers have been able to provision and maintain facilities to deliver high quality telecommunications services to rural consumers through a balanced system of end user rates, intercarrier compensation, and Universal Service Funds. This balance recognizes implicitly that the networks provided by rural carriers are valuable not only to rural subscribers, but also to other carriers that benefit from the opportunity to sell services that require the use of these networks for origination and termination. The proposals and comments of several parties in this proceeding, however, overlook this fact.

There exists no rational basis to undertake changes that would eliminate or substantially reduce intercarrier compensation while significantly increasing both end user rates and the size of the Universal Service Fund. In these Reply Comments, the Rural Alliance provides a quantitative analysis that demonstrates the otherwise unnecessary burden that the proposals of several parties would impose on the Universal Service Fund and end user rates by eliminating intercarrier compensation.

The Rural Alliance is concerned that (1) significant and unnecessary increases to end user rates will result in unaffordable rates in rural areas, and (2) if the Universal Service Fund is expanded beyond what is necessary to achieve an economically efficient and unified intercarrier compensation regime, then the sustainability of the entire Universal Service Funding process could be in jeopardy. Accordingly, the Rural Alliance submits that any successful intercarrier compensation reform must focus on both enforcement *and* changes in current rules in order to ensure that all carriers pay a rational cost-based charge when they benefit from the ability to sell services that require the use of the rural networks. Moreover, the adoption of the approach proposed by the Rural Alliance will properly minimize the impact of changes on both end user rates and the Universal Service Fund, and in so doing will promote and advance Universal Service in rural and high cost areas.

A unified, cost-based intercarrier compensation will provide all carriers, including rural local exchange carriers, with both the incentives and the ability to deliver to rural consumers telecommunications services that are reasonably comparable to those available in urban areas, both in quality and in price. While changes in the intercarrier compensation framework are needed, it is neither necessary nor desirable to eliminate the current system in its entirety and to substitute an untested replacement.

The Rural Alliance submits, and the record supports, that the Commission's intercarrier compensation goals can be achieved, and the impact on the Universal Service Fund and end user rates minimized, by intercarrier compensation changes that adhere to the following principles and conclusions:

1. Uniform application of unified, cost-based rates to all retail service providers that utilize other carriers' networks. For rural carriers operating under rate-of-return regulation, such rates should be based on embedded cost;

2. Compensation for both origination and termination of traffic where carriers providing equal access are required to originate traffic for retail service providers that do not have a physical connection to the end user;

3. Rates converging to common levels, while maintaining access and reciprocal compensation as separate and distinct services;

4. Establishment of a nationwide local service rate benchmark to ensure that all consumers pay reasonably comparable basic service rates;

5. Increase of Subscriber Line Charges for price cap carriers to current cap levels as a means of recovering some or all of intercarrier revenue reductions for those carriers not at the cap.

6. Maintain existing interconnection requirements and meet-points; and

7. Implement rules that minimize "phantom traffic" and ensure that carriers pay for their use of network functionality.

In addition, the evolution of the Internet is a significant driver that demands changes in the current intercarrier compensation framework. The market power enjoyed by Internet backbone providers, as well as by certain tandem owners and transit service providers, could harm rural consumers unless appropriate regulatory safeguards that ensure access to these critical resources under equal terms and conditions and at affordable prices are implemented. The ongoing consolidation within the telecommunications industry underscores these concerns. Consistent with this position, and recognizing the market power advantages that larger carriers possess, the Rural Alliance is strongly opposed to proposals made by several parties that would deregulate intercarrier compensation and transition interconnection arrangements to commercial agreements.

A collaborative process between state and Federal regulators would achieve a unified cost-based intercarrier rate structure. Such a process respects the legal authority of all parties, and has the greatest probability of achieving a sustainable, unified intercarrier compensation regime in the shortest period of time.

To assist the Commission in implementing intercarrier compensation reform, the Rural Alliance has developed a plan that contemplates a collaborative Federal-State effort to establish a unified compensation system.

REPLY COMMENTS
OF THE RURAL ALLIANCE

I. INTRODUCTION

On May 23, 2005, more than 100 parties filed in excess of 3,000 pages of comments in response to the Commission's Further Notice of Proposed Rulemaking (FNPRM or Notice) in this proceeding.[1] A forceful, overarching, and inescapable fact is evident from a review of these comments -- a close relationship exists between the intercarrier compensation issues at stake in this proceeding and the overall issue of Universal Service. Universal Service has been a hallmark of Federal telecommunications policy for more than 70 years. The goals of Universal Service were reiterated and developed further in the Telecommunications Act of 1996 (1996 Act).[2] Any intercarrier compensation reform proposal must be evaluated in the context of how it will affect the maintenance and advancement of critical Universal Service goals, including that of providing broadband connectivity to rural areas.

As discussed in the initial Comments of the Rural Alliance,[3] rural carriers have been able to provision and maintain facilities to deliver high quality telecommunications services to rural consumers through a balanced system of end user rates, intercarrier

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[1] *I/M/O Developing a Unified Intercarrier Compensation Regime: Further Notice of Proposed Rulemaking*, CC Docket No. 01-92, FCC 05-33 (rel. Mar. 3, 2005) (FNPRM).

[2] The 1996 Act amended the Communications Act of 1934. References to the Act in these Reply Comments refer to the Communications Act of1934, as amended, as codified in the United States Code.

[3] The membership in the Rural Alliance currently consists of more than 250 organizations, including individual rural telephone companies as well as associations representing several hundred companies. The current membership in the Rural Alliance is set forth in Appendix A. The Rural Alliance respectfully reserves the right to supplement this list as membership in the Alliance continues to grow during the course of this proceeding.

compensation, and Universal Service Funds.[4] This balance recognizes implicitly that the networks provided by rural carriers are valuable not only to rural subscribers, but also to other carriers that benefit from the opportunity to sell services that require the use of these networks for origination and termination. The proposals and comments of several parties in this proceeding, however, overlook this fact.

Several of the proposals submitted in this proceeding, particularly those that rely in whole or in part on mandatory bill and keep, ignore the current rational balance in network cost recovery. While the Rural Alliance agrees that adjustments to the current intercarrier compensation system are necessary in order to address technological and operational realities, there exists no rational basis to undertake changes that would disrupt this balance by eliminating or reducing substantially intercarrier compensation while increasing significantly both end user rates and the size of the Universal Service Fund. In these Reply Comments, the Rural Alliance provides a quantitative analysis that demonstrates the otherwise unnecessary burden that the proposals of several parties would impose on the Universal Service Fund and end user rates by eliminating intercarrier compensation.

While it is obvious how the elimination of charges for the use of rural carriers' networks would advance the business interests of the parties making suggestions to do so, the impact that such proposals would have on the viability and sustainability of the Universal Service Fund and comparable and affordable end user rates must also be considered. The Rural Alliance is concerned that (1) significant and unnecessary increases to end user rates will result in unaffordable rates in rural areas, and (2) if the

Universal Service Fund is expanded beyond what is necessary to achieve an economically efficient and unified intercarrier compensation regime, then the sustainability of the entire Universal Service Funding process could be in jeopardy. Accordingly, the Rural Alliance submits that any successful intercarrier compensation reform must focus on both enforcement *and* changes in current rules in order to ensure that all carriers pay a rational cost-based charge when they benefit from the ability to sell services that require the use of the rural networks. Moreover, the adoption of the approach proposed by the Rural Alliance will properly minimize the impact of changes on both end user rates and the Universal Service Fund, and in so doing will promote and advance Universal Service in rural and high cost areas.

In these Reply Comments, the Rural Alliance demonstrates that the preponderance of the comments in this proceeding support a unified, cost-based intercarrier compensation regime. Such a properly structured regime would provide all carriers, including rural local exchange carriers (rural LECs), with both the incentives and the ability to deliver to rural consumers telecommunications services that are reasonably comparable to those available in urban areas, both in quality and in price.[5] The Rural Alliance will also present a plan for intercarrier compensation reform that: (1) provides for immediate changes that will address some concerns; (2) enables substantial progress towards establishing a revised framework yet this year; (3) permits implementation of the needed reforms in an orderly fashion; (4) accomplishes the Commission's overall goals;[6]

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[4] Comments of the Rural Alliance at 72.

[5] 47 USC 254(b)(3).

[6] FNPRM at paragraphs 29 through 36.

(5) respects the legal authority of this Commission and the states; and (6) protects the legitimate needs of carriers and consumers.

A complete reading of the comments submitted in response to the FNPRM indicates that while changes in the intercarrier compensation framework are needed, it is neither necessary nor desirable to eliminate the current system in its entirety and to substitute an untested replacement, such as the "Edge" proposal embodied in a number of plans. As set forth in these Reply Comments, the record indicates the following:

- Most parties oppose a mandatory bill and keep system;
- Most parties oppose a radical restructure of current interconnection rules, including meet-points; and
- With a few exceptions, all parties agree that Universal Service must be preserved as intercarrier compensation is modified.

The Rural Alliance's analysis of the proposals included in this proceeding reveals their potentially significant and unnecessary adverse impacts on end user rate levels and the Universal Service Fund. Details of this analysis can be found in section IV.B of these Reply Comments.

The Rural Alliance submits, and the record supports, that the Commission's intercarrier compensation goals can be achieved, and the impact on the Universal Service Fund and end user rates minimized, by intercarrier compensation changes that adhere to the following principles and conclusions:

1. Uniform application of unified, cost-based rates to all retail service providers that utilize other carriers' networks. For rural carriers operating under rate-of-return regulation, such rates should be based on embedded cost;

2. Compensation for both origination and termination of traffic where carriers providing equal access are required to originate traffic for retail service providers that do not have a physical connection to the end user;

3. Rates converging to common levels, while maintaining access and reciprocal compensation as separate and distinct services;

4. Establishment of a nationwide local service rate benchmark to ensure that all consumers pay reasonably comparable basic service rates;

5. Increase of Subscriber Line Charges (SLCs) for price cap carriers to current cap levels as a means of recovering some or all of intercarrier revenue reductions for those carriers not at the cap;

6. Maintain existing interconnection requirements and meet-points; and

7. Implement rules that minimize "phantom traffic" and ensure that carriers pay for their use of network functionality.

The Rural Alliance recognizes that the evolution of the Internet is a significant driver that demands changes in the current intercarrier compensation framework. Accordingly, the Commission's consideration of intercarrier compensation must also include the resulting impact on the availability of Internet-based services in rural and high cost areas. As explained in initial Comments of the Rural Alliance,[7] the market power enjoyed by Internet backbone providers, as well as by certain tandem owners and transit service providers, could harm rural consumers unless appropriate regulatory safeguards that ensure access to these critical resources under equal terms and conditions and at affordable prices are implemented. The ongoing consolidation within the telecommunications industry underscores these concerns. Consistent with this position, and recognizing the market power advantages that larger carriers possess, the Rural Alliance is strongly opposed to proposals made by several parties that would deregulate

[7] Comments of the Rural Alliance at 119, 160. Unless otherwise indicated, citations herein refer to comments filed on or about May 23, 2005, in the instant proceeding.

intercarrier compensation and transition interconnection arrangements to commercial agreements.

Like the Rural Alliance, most parties in this proceeding propose some form of collaborative process between state and Federal regulators in order to achieve a unified cost-based intercarrier rate structure. Such a process respects the legal authority of all parties, and has the greatest probability of achieving a sustainable, unified intercarrier compensation regime in the shortest period of time.

To assist the Commission in implementing intercarrier compensation reform, the Rural Alliance has developed a plan that contemplates a collaborative Federal-State effort to establish a unified compensation system. Under this plan, which is discussed throughout these Reply Comments and described fully in Section VI.B and in Appendix C, the Commission would adopt during 2005 some immediate "fixes" to the current intercarrier compensation regime, outline generally the parameters of a unified intercarrier compensation regime, and instruct both the Federal-State Joint Boards on Separations and Universal Service to develop detailed plans and procedures to implement the unified regime, including incentives for states to opt-in voluntarily to this process. In order to avoid rate shock and preserve equity among the states, the plan also provides for a phased implementation of unified intercarrier rates and benchmark rates for local service. Adoption of this plan would enable the Commission to take decisive action this year to begin the reform process, and to proceed in a logical and collaborative fashion to perform the analysis necessary to address the many complex details contemplated by a new and comprehensive intercarrier compensation plan.

The Rural Alliance also recommends that the Commission examine Internet protocol (IP) interconnection compensation in order to complete the record in this Notice. Doing so will assist the Commission's determination as to what type of intercarrier compensation process should be applied to the Public Switched Telecommunications Network (PSTN) environment, and whether regulatory oversight of IP interconnection is advisable to maintain an open and robust public Internet platform. Another related issue that the Commission should evaluate is cost recovery in an IP environment. Since rural LECs would presumably no longer receive adequate intercarrier compensation payments in an IP environment, there are significant high cost support funding questions that must be considered as communications applications migrate to an integrated-services IP platform.

II. UNIFIED INTERCARRIER COMPENSATION SHOULD BE IMPLEMENTED ON THE BASIS OF COST-BASED RATES, AND NOT ON THE BASIS OF MANDATORY BILL AND KEEP.

Like the Rural Alliance, a large number of the commenting parties support using each carrier's embedded cost to set intercarrier rates.[8] Virtually all commenters recommended that unified intercarrier compensation rates be based upon some measure of cost and only a few parties to this proceeding support a mandatory bill and keep regime. In addition, the National Association Regulatory Utility Commissioners'

[8] *See* Comments of California Small LECs at 6; Coalition for Capacity-Based Access Pricing at 18; ERTA at 2; Interstate Telecom consulting at 19; ICORE at 4; John Staurulakis, Inc. (JSI) at 5; Minnesota Independent Coalition at 17; Montana Information Telecommunications System (MITS), Montana Telecommunications Association (MTA) and Mid-Rivers at 13; National Exchange Carrier Association (NECA) at 14; National Telecommunications Cooperative Association (NTCA) at 32; TCA at 3; and Wyoming Independent Telephone Companies at 5.

(NARUC's) principles state that intercarrier compensation rates should "recover an appropriate portion of the requested carrier's applicable network cost."[9]

A. THE RECORD REFLECTS OVERWHELMING OPPOSITION TO MANDATORY BILL AND KEEP.

A large and diverse group of parties including those representing rural LECs,[10] Regional Bell Operating Companies (RBOCs,)[11] competitive local exchange carriers (CLECs,)[12] state regulators[13] and consumer advocates[14] oppose the application of a mandatory bill and keep regime for intercarrier compensation. Parties opposing bill and keep have highlighted the legal, operational, and public policy flaws associated with the proposal.[15] Rural companies are concerned about the impact that bill and keep would have on end user rates, the size of the Universal Service Fund, and on maintaining an appropriate balance in recovering the cost of operating rural networks from rural end users, intercarrier compensation, and the Universal Service Fund. As stated by the South

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[9] *See* Comments of NARUC at 2.

[10] *See* Comments of CenturyTel at 19; North Dakota Association of Telephone Cooperatives at 5; Coalition for Capacity-Based Access Pricing at 11; CTA-OTA-WITA at 7; Iowa Telephone Association at 4; MITS-MTA-Mid Rivers at 11; NTCA at 17.

[11] *See* Comments of BellSouth at 10-12, Verizon at 23-24.

[12] *See*, Comments of CCG Consulting at 8; Pac West Telecom, *et. al.* at 13-15; PrairieWave at 4, Time Warner Telecom at 30-34.

[13] *See* Comments of Iowa Utilities Board (IUB) at 7; Indiana Utility Regulatory Commission (IURC) at 3; Nebraska PSC at 7; South Dakota PSC at 7.

[14] *See* Comments of National Association of State Utility Consumer Advocates (NASUCA) at 46; New Jersey Ratepayer Advocate at 4; Texas Office of Public Utility Counsel, Consumer Federation of America, and Consumers Union at 3.

[15] *See* Comments of IUB at 7 (a bill and keep system "would be financially disastrous for many rural telephone companies") IRUC at 3 ("a seriously flawed proposal that is not well supported").

Dakota PSC, "one of the best ways to minimize the impact on Universal Service is to keep an access charge and not transition to bill and keep."[16]

Further, it is not surprising that essentially all proponents of bill and keep also advocate Federal preemption of state authority over intrastate access. They advocate that "fixing" intercarrier compensation by eliminating access can be accomplished only by having one overarching regulatory authority (*e.g.*, the Commission) negate the powers of the other authorities (*i.e.*, the states). Such blunt force is unnecessary and legally questionable. Basing any unified intercarrier compensation plan implementation on Federal preemption will, at a minimum, lead to further delay and instability resulting from either legal challenges or a need for statutory changes. Accordingly, the Rural Alliance submits that a collaborative approach to the unification of intercarrier rates is the best approach to implement sustainable intercarrier compensation modifications. The Maine and Vermont Commissions also call for a collaborative approach within existing jurisdictional authority, stating, "In trying to create a rational compensation scheme, the Commission must limit its own actions to the scope of its own authority, and it does not have authority to preempt state jurisdiction over intrastate access."[17] NARUC and various state commissions share the Rural Alliance's views that Sections 251(g) and 254(g) do not provide any basis to extend the Commission's authority to intrastate access.[18] Many regulators also agree that, in addition to being unlawful, preemption would have a destabilizing effect on the industry.[19]

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[16] *See* Comments of South Dakota PSC at 11.

[17] *See* Comments of Maine and Vermont at 4.

[18] *Id.* at 9-11.

The Rural Alliance agrees with other parties that bill and keep is illegal because a "zero" rate cannot meet the additional cost standard. As PacWest *et. al.* state, "Mandatory bill and keep when traffic is out of balance can never satisfy the 252(d)(2) standard."[20] NASUCA agrees, stating "it is difficult to see how [bill and keep's] proposal to lower the reciprocal compensation rate to zero can contain any approximation of additional costs. As a result, [bill and keep], on its face, appears to conflict with Section 252(d)(2)."[21] BellSouth, a former ICF member, captures the situation: "In light of the flaws inherent in bill and keep regimes, including the disincentives to investment, the failure to provide compensation for fair value provided, and the institution of new arbitrage opportunities, a bill and keep default rule for virtually all traffic is not a legally defensible outcome."[22]

B. ADOPTION OF A MANDATORY BILL AND KEEP REGIME WOULD CREATE UNFAIR AND ANTI-COMPETITIVE RESULTS.

The impetus underlying bill and keep must be analyzed in light of the serious political and legal deficiencies that plague the proposal. Primary sponsors of bill and keep include the wireless industry and interexchange carriers. Each of these parties sells services that require the use of the networks of rural LECs to originate or terminate their services, and each of these parties seeks to minimize its expenses associated with the use

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[19] *See* Comments of NARUC at 4; New Jersey Board of Public Utilities (BPU) at 5; Ohio Public Service Commission at 3.

[20] *See* Comments of Pac West, *et al*. at 23.

[21] *See* Comments of NASUCA at 36.

[22] Comments of BellSouth at 23.

of other carrier's networks through imposition of mandatory bill and keep. These industry players are seeking an unwarranted, unfair, and anti-competitive advantage.

The wireless industry is promoting bill and keep in an attempt to limit the reciprocal compensation payments that wireless carriers must make to LECs. The Cellular Telecommunications and Internet Association (CTIA) claims that its plan "provides incentives for efficient and innovative *voluntary* arrangements."[23] Presumably, such voluntary arrangements would not involve any payments for network use. Western Wireless attempts to justify mandatory bill and keep by implying that since the law permits voluntary bill and keep when traffic is balanced, bill and keep is appropriate in all instances.[24] Bill and keep, however, is fair and economically rational only when parties agree *voluntarily* to such arrangements where the net effect of traffic volumes and network costs is relatively balanced.

The interexchange carriers also have clear and obvious economic incentives to promote mandatory bill and keep. These carriers desire Commission approval to use LECs' networks for free, eliminating access expenses when they use LEC networks to originate and terminate services they sell. BellSouth recognizes that the ICF's bill and keep plan is not competitively neutral because it forces LECs to bear the cost of the local network where interexchange calls originate.[25] BellSouth has concluded correctly that the competitive effect of implementing bill and keep would be to advantage carriers that sell services to customers to whom they are not physically connected.

[23] Comments of CTIA at 10, 11 (emphasis added).

[24] Comments of Western Wireless at 16, 17.

[25] Comments of BellSouth at 10.

If the important goals of Universal Service are to be preserved, then all carriers that utilize networks to originate or terminate services that they sell must shoulder the cost of those networks appropriately. The Rural Alliance agrees with the New Jersey Ratepayer Advocate, which stated succinctly, "**Bill-and-keep is neither cost-based nor equitable.**"[26] The self-serving proposals for mandatory bill and keep by interexchange carriers, wireless carriers, and the cable industry would result in unwarranted, unfair, and anti-competitive advantage for those carriers.

[26] Comments of the New Jersey Ratepayer Advocate at 4 (emphasis in original).

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III. THE OUTCOME OF THIS PROCEEDING SHOULD ENSURE THAT ALL CARRIERS PROVIDE EQUITABLE COMPENSATION TO LECs FOR NETWORK UTILIZATION TO ORIGINATE OR TERMINATE SERVICES THEY SELL. THE STRUCTURE FOR COST-BASED UNIFIED INTERCARRIER COMPENSATION RATES SHOULD MAINTAIN THE EXISTING FRAMEWORK WITH APPROPRIATE CLARIFICATIONS AND MODIFICATIONS.

Similar to the underlying approach evident in proposals for mandatory bill and keep, several parties advocate changes to the fundamental intercarrier compensation structure that would clearly benefit their own business interests as well as adverse to the overall public interest and the goals of Universal Service. By contrast, the Rural Alliance demonstrates that appropriate clarifications and modifications to the existing framework are the best way to achieve implementation of a unified intercarrier compensation system. As discussed below:

1. The existing interconnection compensation framework, including assessment of originating access charges when appropriate, should be maintained;
2. The establishment of a unified intercarrier compensation rate should recognize the traffic-sensitive nature of the services provided and, for rate of return LECs, should be based on embedded costs;
3. The clarification of the Commission's existing interconnection rules should provide needed stability during a transition to a unified intercarrier compensation regime; and
4. The implementation of a unified intercarrier compensation regime should include establishing local rate benchmarks to ensure that a balanced

system of end user rates, intercarrier compensation and Universal Service Fund support is maintained.

A. CARRIERS SHOULD COMPENSATE LECS FOR USING THE LEC'S NETWORK TO ORIGINATE OR TERMINATE SERVICES THEY SELL; THE ICF'S "EDGE" SCHEME SHOULD BE REJECTED.

1. Unified Intercarrier Compensation Rates Should Be: Established on an Individual LEC Basis; Applied to All Similarly-Functional Interconnection Services Regardless of Other Distinctions in the Interconnection Services; and Assessed to All Carriers that Require the Use of the LEC's Network to Originate or Terminate Services.

The Rural Alliance with the parties who support a unified intercarrier compensation regime.[27] Ultimately, and as a result of the collaborative Federal-State Joint Board process recommended by the Rural Alliance, unified intercarrier compensation rates that enable each LEC to charge the same rate for equivalent network interconnection functionality can be established, irrespective of whether another carrier's traffic is terminating or originating, reciprocal compensation or access, or interstate or intrastate.

The implementation of a unified rate and a uniform interconnection regime that eliminates disparate regulatory treatment, however, does not mean that all carriers utilize the same rate, whether the rate is zero or some other arbitrary level. Any such requirement would be unlawful to the extent that it prevents a LEC from establishing its

[27] *See*, Comments of BellSouth at 4; NASUCA at 2, 4; NARUC at 3; and CBICC at p. iii.

own cost-based rate.[28] Rates that are not cost-based do not comply with either the additional cost standard in Section 252(d)(2) of the Act or the long-standing regulatory tenet of setting fair, just, and reasonable rates. Moreover, arbitrage and gaming would worsen if rates are not based on cost.

The establishment of a unified rate should not result in the loss of valid distinctions that are current features of interconnection rules. Various parties to this proceeding understand that unification of interconnection rates does not mean that the distinctions between interexchange access and reciprocal compensation must be dissolved.[29] With the exception of the ICF and its supporters, most other parties to this proceeding recognize the basic wholesale/retail business relationship that allows Retail Service Providers (RSPs) including, but not limited to, interexchange carriers (IXCs) to use the LECs' underlying networks to originate and terminate the RSP's retail traffic.[30] The current interconnection rules are rooted in the common-sense principle that the RSP benefits from the use of LECs' networks and creates network cost; therefore, the RSP is responsible for compensating network providers for such use. Consistent with these principles, the Rural Alliance proposal provides for continuation of intercarrier compensation to LECs from all carriers that utilize the LECs' networks to originate and terminate their traffic.

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[28] The Rural Alliance recognizes the continued value of pooling the costs and revenues of incumbent rural LECs. The Rural Alliance proposal supports the continued option to pool costs and revenues as a means to equalize rates in high-cost rural areas of the nation.

[29] Comments of NASUCA at 36; Verizon at 38.

[30] Comments of NASUCA at 25; Verizon at 21; South Dakota PUC at 10; and BellSouth at 17.

In a blatant attempt to eliminate originating interexchange access charges, the ICF argues that the wholesale/retail business relationship between carriers is no longer appropriate and becomes "moot" if the Commission adopts the ICF plan.[31] By eliminating the RSP's compensation obligation, LECs would be required to switch and transport traffic to distant points without compensation. No business or public policy principle could justify a mandate that a service provider incur the cost of delivering the service of another without appropriate compensation.[32] As the Rural Alliance explained in its initial Comments, when an RSP does not have its own physical connection to the customer, originating access charges should continue to be assessed to the RSP.[33] A balanced, economically-efficient, and legally-sustainable compensation regime requires the RSP to compensate the LEC when the RSP requires the use of the LEC's network to originate the services the RSP sells.

The ICF implies that the industry's compensation issues are too difficult to resolve and will result in endless litigation, and that the Commission should therefore abandon the existing retail/wholesale interconnection rules.[34] By contrast, Verizon

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[31] *See* Comments of ICF at 56.

[32] *See* Comments of the Rural Alliance at 98, 100. The Rural Alliance notes that the ICF is also incorrect in its interpretation of the ARIC plan. (The ARIC plan was submitted to the FCC prior to the ARIC and EPG groups joining to form the Rural Alliance.) The Rural Alliance, which includes the ARIC companies, has taken the position that carrier relationships cannot be harmonized under a single network interconnection framework, even though the rates might be unified. The Rural Alliance's position is based on examination of Section 251(g), which addresses access, and Section 251(b)(5), which addresses reciprocal compensation. The provision of transport and termination services to an IXC by a LEC cannot be part of "reciprocal compensation" since there is no reciprocal service; IXCs do not provide transport and termination services to LECs. While the same unified rate can be established for both access and reciprocal compensation, in both instances the RSP remains responsible for compensating the provider of transport and termination services necessary for the RSP to provide its service.

[33] Comments of the Rural Alliance at 13.

[34] Comments of ICF at 56.

observes that the "hotly disputed issues have been resolved."[35] According to the ICF, the "retail/wholesale dichotomy" cannot be maintained as alternatives to traditional landline service, such as wireless and VoIP, emerge because the IXCs cannot compete with other technologies.[36] Despite the possibility that rate unification would likely lower originating access rates, an IXC's competitiveness, or lack thereof, is not a reason to abandon an appropriate business relationship. The ICF also argues that existing rules require regulators to distinguish between calls where the originating LEC is the retail provider and calls where the originating LEC is the wholesale provider. But, there is nothing mysterious or complex about identifying the retail provider. In fact, LECs identify the RSP for all calls traversing their networks today.

The Rural Alliance submits that the Commission's objectives in this proceeding can be accomplished by utilizing the existing intercarrier compensation framework, together with rational clarifications and modifications as discussed below. Other parties, recognizing the necessity of maintaining and enforcing a compensation obligation by RSPs that use the LECs' facilities to provide end-to-end service, also support fully the continuation of terminating and originating rates.[37] The comments of these parties,

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[35] Comments of Verizon at 29.

[36] Comments of ICF at 56.

[37] *See* Comments of BellSouth at 26; California Small LECs at 6 ; CenturyTel at 27; CTA, OTA and WITA at 25; ERTA at 3; Great Lakes Comnet at 6; GVNW at 16; IUB at 2; ICORE at 3-4; Iowa Network Services at 6; Indiana Consumer Council at 2; Interstate Telecom Consulting at 16; KMC Telecom/Xspedius at 28; MITS, MTA, and Mid-Rivers Telecommunications Cooperative at 13; Minnesota Independent Coalition at 10 and 17; NASUCA at 2; NCTA at 3-4; North Dakota Association of Telephone Cooperatives at 8; Nebraska Public Service Commission at 6; NTCA at 14; SureWest Communications at 12; TCA at 3; TDS Telecom at 16; Consumer Federation of America and Consumers' Union at 7; Wisconsin Telecommunications Association at 2.

together with those of the Rural Alliance, demonstrate that a proposal to eliminate originating access charges, such as that set forth in the ICF's plan, should be rejected.

2. The ICF's "Edge" Interconnection Proposal is Harmful to All But the Largest Carriers.

The ICF "Edge" interconnection scheme would eliminate inequitably originating access compensation obligations and impose uneconomic requirements on rural LECs and other smaller carriers by requiring all carriers to establish network "Edges" at which they would meet other carriers. The "Edge" proposal not only imposes unreasonable network obligations on small carriers, but also affects severely and adversely the provision of Universal Service. Under the "Edge" scheme, cost recovery for switching and transport would either be recovered from already-stressed Universal Service mechanisms or foisted upon end users, while the RSP that utilizes those facilities would pay nothing.

As the Rural Alliance highlighted in its initial Comments, the ICF plan would illegally apply reciprocal compensation obligations under Section 251(b)(5) to interexchange access.[38] As the Maine Commission and Vermont Board note, the LECs have never established reciprocal compensation arrangements with interexchange carriers, and Congress distinguished specifically exchange access service from reciprocal compensation transport and termination arrangements.[39] The "Edge" plan conveniently ignores that: (1) there is no "reciprocal" arrangement between LECs and interexchange carriers; and (2) an RSP that does not have facilities physically connected to its customer

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[38] Comments of the Rural Alliance at 113.

[39] Comments of Maine Public Utilities Commission and the Vermont Public Service Board at 7.

requires the use of LECs' networks to switch and transport the RSP's service.[40] Neither statute nor rhetoric can justify a requirement that a LEC provide its network to an RSP free of charge.

Other parties share the Rural Alliance's viewpoints on the inappropriateness and illegality of the ICF "Edge" plan to eliminate originating access responsibilities. Former ICF members BellSouth[41] and Verizon advocate maintenance of existing physical interconnection arrangements so as not to disrupt existing connections or force major physical network rearrangements. Verizon contends that simultaneous introduction of radical changes to both interconnection and intercarrier compensation would exacerbate arbitrage opportunities.[42]

3. The Concerns Expressed by State Regulators Further Demonstrate that the "Edge" Plan Should Be Rejected and that Intercarrier Compensation for Originating Interexchange Access Services Should Be Maintained.

In comments filed by NARUC, state regulators demonstrated concerns for their rural constituents similar to those expressed by the Rural Alliance regarding the preservation of exchange access distinct from Section 251(b)(5) reciprocal compensation. NARUC, like the Rural Alliance, pointed out that the legislative history of the Act reflects Congress' intent not to disturb the exchange access regime. NARUC also

[40] Comments of the Rural Alliance at 113.

[41] *See* Comments of BellSouth at 17. BellSouth offers a new proposal whereby IXCs pay originating and terminating compensation at a unified level. The Rural Alliance, however, opposes the general imposition of BellSouth's proposed default Average Traffic Sensitive Rate ("ASTR") of $0.00125, as it is significantly under the cost of transport and termination for rural LECs.

[42] *See* Comments of Verizon at 30-33.

recognized the ICF's "distortions" in attempting to apply Section 251(b)(5) to exchange access.[43]

While NARUC's legal position demonstrates the fallacy of the ICF "Edge" proposal's foundation, the NARUC Intercarrier Compensation Task Force Proposal (NARUC Version 7 Proposal) tentatively adopts the ICF's "Edge" proposal, subject to conditions for further exploration or discussion.[44] The NARUC Version 7 Proposal includes two alternatives regarding origination rates: one without an originating rate, and the other with a rate of $0.002 per minute where equal access obligations are required by law.[45] The Rural Alliance respects the attempt of the NARUC Intercarrier Compensation Task Force to find compromise positions among diverse interests. NARUC's proposals, however, do not address the fundamental flaw in the "Edge" scheme: carriers should not be given free (or under-priced) rides on rural LEC networks when those networks are used to switch and transport the services of RSPs. These proposals are inconsistent with the very principles that NARUC has wisely adopted.[46]

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[43] Comments of NARUC at 7-8.

[44] *See* NARUC Version 7 Proposal at 13 (May 17, 2005). The proposal does recognize that if changes to the ICF edge proposal are necessary to permit an origination charge, such changes will require further discussion.

[45] *Id*, at 3, 4.

[46] Although the Rural Alliance appreciates the effort of NARUC to recognize the continuing need for an originating access charge, the proposed second alternative, which includes an arbitrary originating rate of $.002 per minute, is not reflective of the costs of providing service in rural LEC service areas. In fact, this proposed rate is well under the tiered termination rates for smaller wire centers set forth in the same proposal. As a result, implementation of this alternative does *not* "charge the same amount to all Covered Entities to whom the service or function is being provided" (NARUC Principle III C), nor does the rate cover "an appropriate portion of the requested carrier's applicable network cost" (NARUC Principle III B).

As set forth in its initial Comments, the Rural Alliance submits that the comprehensive implementation of a unified intercarrier compensation regime must be a collaborative process between the Commission and state regulators.[47] The Rural Alliance further submits that in order to fully serve the public interest, the result of the anticipated collaborative process should incorporate revisions to the NARUC Version 7 Proposal that provide for a unified originating and terminating cost-based rate and adhere to existing interconnection rules. This recommendation is consistent not only with the public interest, but also with the common interests of state regulators and the rural customers they serve.

B. A UNIFIED INTERCARRIER COMPENSATION RATE MUST MAINTAIN THE USE OF EMBEDDED COSTS AND RECOGNIZE THE TRAFFIC-SENSITIVE NATURE OF THE SERVICES PROVIDED.

The Rural Alliance proposes the continued utilization of embedded cost to develop unified intercarrier compensation rates applicable to both exchange access and reciprocal compensation for rural LECs. The identification of interconnection costs and the establishment of a unified rate are consistent with both the applicable statutory rate standard and existing Commission rules and regulations.[48] Moreover, the Rural Alliance proposal avoids the sophistry of debating economic theory while addressing the realistic need to maintain a rational cost recovery balance between end user rates, intercarrier compensation, and Universal Service Funding. In addition to the utilization of embedded costs, the Rural Alliance proposal recognizes that: (1) achieving the benefits of a unified

[47] Comments of the Rural Alliance at 139-155.

[48] Comments of the Rural Alliance at 42.

intercarrier compensation rate does not require the same rate for all carriers; and (2) the traffic-sensitive nature of the interconnection service should be recognized in pricing.

1. Embedded Costs and Existing Part 36 and 69 Rules Should Be Used to Establish Intercarrier Compensations Rates for Rate of Return Companies.

While the record in this proceeding reveals an overwhelming opposition to adopting bill and keep as the appropriate intercarrier compensation regime, there is less clarity in commenters' responses to the Commission's inquiry regarding the application of the appropriate cost standard to the pricing of a unified intercarrier compensation rate.[49] The lack of clarity is not surprising, given that public policy and legal arguments often shroud parties' true business objectives. Nowhere is this theme more evident than in the discussions of economic costing theories wherein parties advocate their theories as "sound economics" simply to achieve lower expenses related to their interconnection with rural LEC networks.

As discussed by the Rural Alliance and others in their initial comments[50] the most accurate and efficient means of establishing intercarrier compensation rates is to use the actual accounting costs of a company *i.e.,* embedded costs. Embedded costs are developed based on rules prescribed by the Commission and the accounting industry's Generally Accepted Accounting Principles (GAAP).

[49] *See FNPRM* at paras. 71-73.

[50] *See* Comments of the Rural Alliance at 34; Iowa Telecommunications Assoc. at 4; Wyoming Independent Telephone Companies at 5; Minnesota Independent Coalition Comments at 17; CTA-WTA-OITA at 25; NTCA at 32; NECA at 14; and ERTA at 2.

(a) Established Rules Can Be Utilized to Establish Unified Intercarrier Compensation Rates.

Specifically, the Rural Alliance proposes that, for rate-of-return carriers, switched-service rate levels be established using embedded costs (using Part 36 and 69 principles).[51] By utilizing embedded costs, the required inputs can be easily identified, audited, and tracked back to actual accounting records of a company, thereby maintaining accountability within the process.[52] Rates based on embedded cost preserve the vital link between investment in and maintenance of rural networks, resulting in comparable services being provided in rural and urban areas, as required by the Act.[53]

(b) With Respect to The Rural LECs, the Utilization of Costing Methodologies Other Than Embedded Costs is Uncertain, Unreliable, and Unproven.

A number of parties advocate the use of alternative costing methodologies to advance special interests and agendas. Some alternative costing methodologies include Total Element Long-Run Incremental Cost (TELRIC), Long-Run Marginal Cost, or

[51] The Rural Alliance understands that price cap companies might not be conducting embedded cost studies in accordance with Parts 36 and 69. The Rural Alliance does not suggest that price cap companies reinstitute Part 36 and 69 studies. Instead, the processes that already apply to price cap companies with respect to adjustments in their rates may be utilized for the establishment of unified intercarrier compensation rates.

[52] The Rural Alliance is not alone in recognizing the value of using embedded costs for the establishment of unified intercarrier compensation rates for rural rate-of-return carriers. For example, Interstate Telecom Consulting observes that embedded costs "represent the actual dollar outlays made for the equipment and services, and can be readily calculated and verified from invoices, contracts and other reliable business documents specifying the prices and terms of arms' length transactions between the 'last mile' carrier and its vendors." Comments of Interstate Telecom Consulting at 19. CTA-WTA and OITA state that "rates should be cost based using each carrier's embedded costs as the basis for the calculation, which accurately reflects the actual cost of the rural network. For rural telephone companies, this is the only cost standard that has ever been shown to work." *See* Comments of CTA-WTA-OITA at 25.

[53] 47 USC 254(b)(3).

Forward-Looking Economic Cost (FLEC). Since these costing terms are imprecise, their results are subject to interpretation and have little meaning without further explanation and specification.

The prevailing assumption underlying the proposal to use alternative costing methodologies appears to be that economic or hypothetical cost standards will produce “more efficient” rates that are lower than today’s access rates. This hypothesis has not been proven for companies providing service primarily in rural service areas. In fact, if costs are properly calculated with reasonable inputs, then the results are often similar to embedded costs. As shown in recent years, hypothetical costing models developed using so-called economic cost standards can be manipulated to derive desired results with significant variation between states.

Hypothetical cost proxy model approaches have proven inconsistent in estimating rural companies’ costs.[54] The Commission itself pointed out the problems associated with the use of its TELRIC rules.[55] As the Rural Alliance noted in its Comments, former Commissioner Furtchgott-Roth questioned whether the use of hypothetical economic cost models promote network efficiency, particularly in rural areas.[56] When the Rural Task Force (RTF) was created, the Commission also recognized that cost proxy models

[54] The Rural Alliance is not alone in pointing out the inaccuracies created when cost proxy models are used to estimate the forward-looking costs of rural carriers. For example, the California Small LECs state, “cost proxy models, which are the primary tools available to calculate forward-looking costs, have proven unreliable in estimating costs for rural companies. The Commission indicated that it would not use such a model to determine support for rural carriers until it had ‘…sufficient validation that forward-looking support mechanisms for rural carriers produce results that are sufficient and predictable.’ None of the submissions in this docket provide the Commission adequate assurance that a cost proxy model applied to rural carriers can meet the Commission’s standard.” California Small LECs at 7.

[55] *See* Comments of the Rural Alliance at 40.

developed for non-rural USF distributions produced unreliable results for rural companies.[57] The RTF agreed that when forward-looking proxy models were applied to rural companies produced faulty results. Parties advocating the application of forward-looking costs to rural LECs have either forgotten or chosen to overlook the RTF findings and the Commission's own concerns.

(c) Proposals to Base Intercarrier Compensation Rates on Either Large Carrier Rates or "Market" Pricing Are Contrary to the Statutory Requirement to Base Rates on the Providing Carrier's Costs. "Market Based" Proposals Subject Interconnection to Market Power Abuse and Distort the Proper Balance of End User Rates, Intercarrier Compensation, and USF.

Instead of using economic costing methodology, several parties would establish intercarrier compensation pricing on a basis that disregards a carrier's cost of providing service. Several parties propose that the Commission adopt arbitrary pegged rate levels for intercarrier compensation and apply those rates on a nationwide basis.[58] Worse yet is the suggestion to negotiate interconnection pricing through "commercial agreements," thereby disregarding the large carriers' potential for market power abuse.

The suggestion that rates be set arbitrarily reflects a misunderstanding of what is meant by a "unified intercarrier compensation regime." Unification of rates means that an individual carrier charges the same rate for equivalent network functionality it

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[56] *See* Comments of the Rural Alliance at 36, 37. The Rural Alliance pointed out concerns over proxy models voiced by others.

[57] *See* "Federal-State Joint Board on Universal Service Announces the Creation of Rural Task Force: Solicits Nominations for Membership on the Rural Task Force." Public Notice, FCC 97J-1 (rel. Sep. 17, 1997).

[58] *See, e.g.,* Comments of BellSouth at 22; NASUCA at 4; NARUC ICC Proposal Version 7 at 4; T-Mobile at pp. 8-17; and Pac-West and US LEC at 11.

provides, no matter if the traffic is terminating or originating, reciprocal compensation or access, or interstate or intrastate. Unification of rates does *not* mean that each carrier would charge the same rate. BellSouth concludes erroneously that rates based on its own costs would be a good proxy for the entire nation.[59] While this proposal may suffice for BellSouth, which has the ability to blend the costs of serving rural areas with the far lower costs of serving densely populated metropolitan areas, BellSouth's costs have no relevance to rural carriers. Rates created on this basis would reflect cost only by accident. Furthermore, low, arbitrarily-set rates will unnecessarily increase end user rates and Universal Service Funding to potentially unsustainable levels.

Verizon goes one step further and ignores completely rural carrier costs in a clear attempt to foster only its own interests. Verizon proposes to set interconnection rates based on "perceived value" instead of any reasonable measure of cost.[60] Disregarding the foundational concept that Universal Service provides value to the *entire* telecommunications system, Verizon argues that different interconnecting networks have different values and that the proper value determination will be realized through negotiated commercial agreements. To permit a large carrier such as Verizon to denigrate the value of universal connectivity is unfathomable. In such an environment, rural customers and carriers would be forever disadvantaged. The Rural Alliance maintains that the use of unregulated, negotiated commercial agreements for network interconnection (based on any technology) is not a prescription for economic efficiency,

[59] *See* Comments of BellSouth at 27.

[60] *See* Comments of Verizon at 16.

but rather for the exercise of market power and a threat to core Universal Service principles.

By contrast, the Rural Alliance's proposal: (1) is administratively simple because it continues the use of embedded costs to establish unified intercarrier compensation rates; (2) is built upon existing costing procedures and network interconnection rules; and (3) can be implemented in a timely manner. Rates established using this methodology can be uniformly applied to all intercarrier compensation services, including Section 251(b)(5) reciprocal compensation and exchange access.

2. Interconnection Costs Are Traffic Sensitive.

(a) Increases in Interconnection Usage Result in Increased Costs.

In considering how rates should be set, the Commission asked whether it should define more precisely which costs are traffic sensitive and thereby recoverable through reciprocal compensation, and which costs are "non-traffic-sensitive."[61] The Commission also noted that a number of parties to the TELRIC proceeding argued that the ". . . majority of switching costs do not vary with minutes of use (MOU) and that switching should be offered on a flat-rate basis rather than a per-minute basis."[62] The Commission also recounted that a number of state commissions have found end-office switching costs to not be traffic sensitive.[63] The Commission asks whether it should reach a similar result

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[61] *See* FNPRM at para. 72.

[62] *See* FNPRM at para. 67.

[63] *Id.*

with respect to recovery of switching costs for purposes of reciprocal compensation.[64] As the Rural Alliance and other parties[65] observed, shared network resources are often traffic sensitive, as increased usage usually requires installation of additional network resources to meet demand.[66]

Certain of the parties to this proceeding attempt to utilize this forum to advance business objectives by offering proposals and arguments that are inconsistent with common operational reality. For example, Nextel Partners claims that switch prices are based on the number of lines served, rather than the number of minutes processed by the switch.[67] Based on this erroneous assumption, Nextel Partners mistakenly concludes that end-office switching costs are not traffic sensitive and, therefore, should not be recovered through reciprocal compensation rates.[68]

The premise that switching costs are not traffic sensitive is not only factually incorrect, but is also indicative of flawed logic. NASUCA indicates that in recent unbundled network element (UNE) cost dockets, incumbent LECs provided evidence showing that some switch vendor contracts charge for switches based on the individual

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[64] *Id.*

[65] Time Warner Telecom also indicated that previous findings of the Commission have held that the use of a network component causes a carrier to incur usage-sensitive costs if (1) the component of the network is shared; or (2) there is an additional cost incurred by each increment of use, since capacity must eventually be expanded to accommodate peak-load demand. *See* Comments of Time Warner Telecom, Conversent Communications, Inc., Cbeyond Communications LLC, and Lightship Telecom ("Comments of Time Warner Telecom") at 11.

[66] *See* Comments of the Rural Alliance at 50.

[67] *See* Comments of Nextel Partners Inc. at 13.

[68] *Id.* at 14.

components ordered, rather than on a per line basis.[69] BellSouth noted that multiple variables must be considered in conjunction with overall network needs, and that in order to obtain the required interfaces, switch components must be purchased on an *à la carte* basis.[70] It is clear, then, that switch prices are not always quoted on a per-line basis; even if they were, it is not a valid basis for concluding that switches are not traffic sensitive.

Several parties explained that the usage of a switch drives costs irrespective of how a vendor may express its pricing. The fact that vendors quote switch prices using per-line proxies does not mean that switches are not traffic sensitive. This information is not new to the Commission.[71] Even MCI, which historically argued that switching is not traffic-sensitive, has recognized previously that vendors' switch pricing on a per line basis is driven by competitive concerns.[72]

Parties attempting to justify that switching costs are not traffic sensitive also argue that switches generally have substantial excess capacity. These parties conclude incorrectly that increases in usage do not increase switching costs. In response to this argument, NASUCA observes that:

> [t]he fact that modern switches often have excess processing capacity does not force the conclusion that capacity costs are NTS [non-traffic-sensitive]. Such a conclusion utterly fails to recognize the reasons why

[69] *See* Comments of NASUCA, Attachment 4, Affidavit of David J. Gabel ("NASUCA, Att. 4") at para. 29.

[70] *See* Comments of BellSouth Corporation at 25.

[71] For example, in the TELRIC proceeding, BellSouth indicated that the equivalent line calculation used in contracts for switches is based on the type of termination and anticipated usage. *See I/M/O Review of the Commission's Rules Regarding the Pricing of Unbundled Network Elements and the Resale of Service by Incumbent Local Exchange Carriers: Reply Comments of BellSouth*,, WC Docket No. 03-173, ("*BellSouth TELRIC Reply Comments*") (Jan. 30, 2004) at 69.

[72] *See I/M/O Review of the Commission's Rules Regarding the Pricing of Unbundled Network Elements and the Resale of Service by Incumbent Local Exchange Carriers: Comments of MCI*, WC Docket No. 03-173, at p. 29, footnote 16, (Dec. 16, 2003) (emphasis added).

> modern switches have been engineered with so much capacity in the first place.[73]

NASUCA also explains that during the early 1990s, when access to the Internet through dial-up connections was growing rapidly, the increased traffic often caused congestion and blocking at the switch; additional capacity was needed to handle the increase in calling and/or longer hold times.[74] The purchase of additional capacity would not have been required if switches were not traffic sensitive.

The Commission suggests that capacity constraints may become obsolete as carriers migrate to Internet-protocol switching, noting the significant capacity of a new router introduced by Cisco Systems.[75] To the contrary, the evidence provided in the initial round of comments demonstrates that switching costs will become even more traffic-sensitive in the future.[76] NASUCA observes correctly that this issue cannot be overly simplified by focusing only on router capacity because in a converged network, there will be a wide range of disparate real-time uses (*e.g.,* video-conferencing) with stringent requirements in terms of delay, jitter, and packet-loss, while others (*e.g.* web

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[73] *See* Comments of NASUCA, Attachment 4 at para. 37.

[74] *Id.*

[75] FNPRM at para. 69.

[76] *See* Comments of NASUCA, Attachment 4 at para. 39. NASUCA notes that an increasing percentage of customers are connected to the switch via digital line carrier (DLC). NASUCA indicates that for a sample switch, the concentration of traffic through the use of DLCs causes the percentage of costs associated with line equipment to decrease, and the percentage of costs associated with shared resources to increase. Therefore as the use of DLCs throughout the network increases, the proportion of switching costs that are traffic-sensitive will increase. NASUCA, Attachment. 4 at paras. 50, 51. The estimates were developed for a Northern Telecom DMS-100, one of the two most commonly used circuit switches in the United States. The #5ESS, the other most commonly used circuit switch, is even more traffic sensitive than the DMS-100.

browsing or e-mail) can be performed easily through best-effort protocols.[77] The cumulative effect of all these uses of the next-generation packet-switching network will result in ever-increasing capacity demands on the network, and as a result, the packet network will likely be more traffic sensitive and capacity constrained than in the PSTN.[78]

In addition to the traffic sensitive nature of switching costs, the Rural Alliance submits that the cost of transport associated with interconnection is also traffic sensitive. GVNW and NTCA explained in their respective comments that transport costs are traffic sensitive because additional trunks and terminals are required as traffic increases.[79] Since transport trunks and terminals are shared, and not dedicated to individual users, the associated cost is considered traffic sensitive.[80]

Transport costs are also distance sensitive, as the majority of transport costs are incurred on a per-mile basis.[81] Rural carriers' transport costs are generally greater than non-rural carriers' costs because of the low density of the area served; traffic must be transported over much greater distances with a much lower traffic volume per mile of transport facility.[82] Arguments that attempt to justify the non-traffic sensitive or non-

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[77] *Id.* at para. 65.

[78] *Id.* at para. 69. NASUCA explains that in order to manage cost effectively with such a mix of traffic, quality of service ("QoS") mechanisms will be necessary to assign the highest performance protocols to be delivered only to the proportion of traffic that requires such treatment. Another approach that can used to deliver multiple services over a converged network is to push the network intelligence further out be towards the network edge. Distributing network intelligence towards the edge allows for more dynamic management of bandwidth routing between different devices in the network, and for capacity allocation among different applications and classes of users.

[79] *See* Comments of GVNW Consulting, Inc. (GVNW) at 39, and NTCA at 39.

[80] *See* Comments of NTCA at 39.

[81] *See* Comments of GVNW at 39.

[82] *See* Comments of NTCA at 39, GVNW at 39.

distance sensitive nature of transport have no basis in fact. Parties advancing such arguments are simply seeking to avoid payment for use of another carrier's switch and transport facilities — costs directly caused by the carriers' use of those facilities and for which appropriate compensation should be provided.

(b) The Traffic Sensitive Nature of Interconnection Costs Does Not Dictate the Pricing Structure, Which May Be Minute-Based or Capacity-Based.

The Rural Alliance recognizes that some parties may benefit by consideration of a capacity-based intercarrier compensation rate structure. Although the Rural Alliance submits that intercarrier compensation rates must be based on a carrier's embedded costs and reflect the traffic-sensitive nature of interconnection, the proper identification of interconnection costs does not necessarily require the maintenance of a rate design based on a per-minute-of-use charge.

A diverse group of parties has proposed the consideration of capacity-based intercarrier compensation plans.[83] Recognizing the changing nature of the telecommunications network, NASUCA states "[I]t appears that as the network evolves … more of the network's costs will be related to the cost of interconnection. This means that it may be appropriate to move recovery of at least a portion of ICC rates to a capacity basis."[84] Many practical problems, however, must be solved before a capacity-based pricing solution could be implemented. For example, PacWest *et. al*. states,

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[83] *See*, *e.g.* Comments of Coalition for Capacity-based Access Pricing at 5; Frontier Communications at 7 and Appendix; Comporium at 7; Minnesota Independent Coalition at 33; JSI at 7; Time Warner Telecom at 8; Small Business Administration at 13; Missouri PSC at 11; IUB at 2.

[84] *See* Comments of NASUCA at 27.

"Commenting CLECs are not opposed to capacity-based charges in lieu of per-minute charges, but the Commission should realize that capacity-based port charges have problems of their own."[85] Given the strong support in the record for further examination of capacity-based pricing, the Rural Alliance recommends that the Commission issue a Further Notice of Proposed Rulemaking to investigate the efficacy of permitting LECs to choose an alternative, capacity-based pricing structure for switched interconnection. This alternative would allow LECs to convert from the per-minute rate structure to a capacity-based rate structure.

C. CLARIFICATION OF THE COMMISSION'S EXISTING INTERCONNECTION RULES WILL PROVIDE NEEDED CERTAINTY DURING A TRANSITION TO A UNIFIED INTERCARRIER COMPENSATION REGIME.

The FNPRM addresses a number of pending issues associated with intercarrier compensation, including matters raised by parties in requests for declaratory rulings. The Rural Alliance respectfully submits that these issues – and the requisite need for clarification – arise because the Commission's interconnection rules are misapplied and obfuscated. These issues surfaced initially in the context of interconnection negotiations where a CMRS carrier sought to impose on rural LECs obligations that simply do not and should not exist.

[85] *See* Comments of PacWest *et. al*. at 15.

1. The Commission Should Affirm That Rural LECs Are Not Required to Route Calls to Points of Interconnection (POIs) Located Beyond Their Local Exchanges or to Assume Responsibility for the Transport of Traffic to Distant Locations Beyond Their Existing Network Boundaries.

Several CMRS providers ask the Commission in their Comments to affirm a "single POI" requirement.[86] As explained in the initial Comments of the Rural Alliance, the so-called "single POI" concept as described by these carriers not only does not exist, but is also contrary to existing law and regulations. Furthermore, if this concept was applied in the manner desired by the CMRS providers, extraordinary costs would be imposed on rural LECs beyond that which any sound policy considerations could support.[87] While the contorted "single POI" theory proffered by the CMRS providers most certainly serves their business interests by inappropriately reducing their interconnection expenses, it disserves the fundamental objectives of Universal Service as it imposing costs on rural carriers by requiring them to route and transport traffic to points beyond their existing networks.[88] A rural incumbent LEC has no obligation to interconnect with carriers at a geographic point where the LEC does not provide local exchange carrier service.[89]

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[86] *See, e.g.,* Comments of Nextel Communications, Inc. at 31; Dobson Cellular Systems and American Cellular Corporation at 4; and Allied National Paging Association at 7. Nextel calls the so-called single POI concept only a "convention."

[87] Comments of the Rural Alliance at 103-106.

[88] Sec. 251(c)(2)(B) of the Act requires a non-rural incumbent LEC to establish a POI at any technically feasible point within its network. Rural LECs that are exempt from Sec. 251(c) pursuant to Sec. 251(f)(1) provide interconnection to requesting carriers at established or mutually agreed upon POIs within the Rural LEC's network.

[89] 47 USC 251(h)(1)-(1)(A) and 47 CFR 51.5 and 51.305(a)-(a)(2).

2. The Commission Should Reject the Attempts by CMRS Providers to Impose on Rural LECs Rating and Routing Requirements That Do Not Exist.

The Commission should reject the attempts by CMRS providers to impose on rural LECs so-called rating and routing requirements that do not exist. CTIA states that the Commission should require a LEC "to load wireless carrier numbers with different routing and rating points into its switches and route calls to those numbers accordingly."[90] CTIA's attempt to carve further advantages for its member CMRS providers is reflective of an ongoing wireless industry effort to inappropriately reduce interconnection expenses by imposing contorted inequitable interpretations of interconnection requirements on rural LECs.

While CMRS providers exercise the right to choose how they interconnect traffic to a rural LEC, they would like to control how the rural LEC sends traffic to them. The wireless carriers apparently want to avoid the expense of establishing a POI within the networks of rural LECs and instead require rural LECs to take financial responsibility for transporting traffic to points beyond their networks. In addition to imposing this inequitable expense on the rural LEC, the CMRS providers want to direct how the rural LEC charges for calls from its wireline customers to the customer of the CMRS provider.

The wireless industry effort (echoed by the CTIA contention referenced above) is part of an effort the CMRS providers initiated within this proceeding when they failed to force rural LECs into acquiescing to their interconnection demands in the course of

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[90] Comments of CTIA at 29.

interconnection negotiations.[91] The CMRS carriers essentially have asked the Commission to condone their notion of interconnection obligations that simply do not and should not exist.

There are no existing requirements for a rural LEC "to load wireless carrier numbers with different routing and rating points into its switches and route calls to those numbers,"[92] as the CTIA and its members have suggested. If a call originating on a LEC network is destined to a terminating point within the LEC's local calling area, then there is no basis to require the originating LEC to route the calls to an interexchange service point that would accommodate the CMRS providers' desire to reduce their interconnection expenses. The wireless carriers seek, essentially, an inequitable Commission ruling that rural LECs must obtain services from a third-party transport provider beyond the LEC's network; take financial responsibility for the transport of the call to a distant location; interconnect with wireless carriers at points well beyond their local exchange service calling areas; and include these calls to a wireless carrier as a local service offering for their LEC end users. No such rule or requirement exists, and as set forth in the Comments of the Rural Alliance, such requirements would be inconsistent with controlling law and policy.[93]

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[91] *See, I/M/O Obligations of Incumbent LECs to Load Numbering Resources Lawfully Acquired and to Honor Routing and Rating Points Designated by Interconnecting Carriers: Sprint Petition for Declaratory Ruling* (May 9, 2002) (Sprint Petition) in this docket. For a more extensive discussion of the issues associated with so-called "routing and rating," *see* Comments of the Alliance of Incumbent Rural Independent Companies and the Independent Alliance filed August 8, 2002, in this docket in response to the Sprint Petition.

[92] Comments of CTIA at 29.

[93] Comments of the Rural Alliance at 103-106.

In an attempt to support the business efforts of its members to reduce interconnection expenses by imposing burdens on rural LECs, CTIA directs the Commission's attention to a rule that simply describes the rights of carriers to obtain numbers and the manner in which numbering resources are to be administered.[94] The rule referenced by CTIA (47 CFR 51.15(g)) describes the general requirements for applying for numbering resources. This rule in no way addresses, let alone dictates, how a LEC is to provision its own local exchange services; whether a LEC is required to route a call in any particular manner; or whether a LEC must include a call to a particular NPA-NXX within its local exchange calling area.

The Rural Alliance respectfully submits that the public interest would be well served by the expedient rejection of the Sprint Petition and the related attempts by wireless carriers to impose new routing and rating requirements on the rural LECs.

3. Interexchange Carrier Service Calls Are Not Within the Reciprocal Compensation Framework that Applies to Local Exchange Service Calls. All Interexchange Carrier Service Calls Are Subject to the Framework of Access.

As the Commission recognized previously, Congress intended that the existing access arrangements of incumbent LECs on the date immediately preceding the date of enactment of the 1996 Act be maintained until superseded explicitly by new rules.[95] The Commission also stated that "the reciprocal compensation provisions of section 251(b)(5) for transport and termination of traffic do not apply to the transport and termination of

[94] CTIA at 29.

[95] *I/M/O Implementation of Local Competition Provisions in the Telecommunications Act of 1996: Order on Remand and Order*, 16 FCC Rcd 9151, 9167 (2001) ("*Section 251(g) Decision*") (para. 34).

interstate or intrastate interexchange traffic."[96] The Commission also rejected the suggestion that the Section 251(b)(5) reciprocal compensation framework applies "when a long-distance call is passed from the LEC serving the caller to the IXC."[97] More significantly, the Commission stated explicitly that "under [its] existing practice, most traffic between LECs and CMRS providers is not subject to interstate access charges *unless it is carried by an IXC . . . .*"[98]

Four years later, the Commission recognized that the access charge framework applies to IXC traffic even when both end users are located within the same MTA:

> Pursuant to Section 51.703(b), a LEC may not charge CMRS providers for facilities used to deliver LEC-originated traffic that originates and terminates within the same MTA, as this constitutes local traffic. Such traffic falls under reciprocal compensation rules if carried by the incumbent LEC, *and under access charge rules if carried by an interexchange carrier.*[99]

In the face of these requirements, some CMRS providers argue that the LEC that provides originating access service to an IXC should be responsible for payment of reciprocal compensation to the CMRS provider when the IXC terminates an IXC call to

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[96] *I/M/O Implementation of the Local Competition Provisions of the Telecommunications Act of 1996: First Report and Order,* CC Docket No. 96-98, FCC 96-325, at para. 1034 (rel. Aug. 8, 1996).

[97] *Id*.

[98] *Id*. at para. 1043 (emphasis added).

[99] *See In the Matters of TSR Wireless, LLC, et al., Complainants, v. US West Communications, Inc. et al., Defendants*: *Memorandum Opinion and Order*, File Nos. E-98-13, E-98-15, E-98-16, E-98-17, E-98-18 (rel. Jun. 21, 2000) at para. 31 ("*TSR Order*") (emphasis added). *See also First Report and Order* at 11 FCC Rcd 16016-17 (paras. 1041-45). The *Section 251(g) Decision* also concluded that traffic subject to access charges is not within the scope of Section 251(b)(5) of the Act. Also, an IXC call is not originated by a LEC, it is originated by the IXC service provider that utilizes the access services of the LEC. The IXC is the originating carrier.

the CMRS provider. For a call beyond the LEC's local calling area, however, toll dialing parity and equal access require that the LEC deliver the call to the interexchange carrier of the customer's choice. For these calls, the IXC is the retail service provider to the end user; the IXC routes and rates the call; the IXC is the entity that determines the terms of service and charges for the call; the IXC bills the end user for the provision of the retail service; and it is the IXC that receives the revenues to compensate the terminating carrier (including CMRS carriers) for the termination of the IXC retail call. The LEC has no responsibility to compensate the CMRS providers for interexchange calls and there is no 251(b)(5) reciprocal compensation obligation on the part of the LEC.

CMRS providers should collect from IXCs terminating charges for IXC calls that terminate to CMRS providers' wireless users. However, some of the CMRS providers suggest that the LEC that provides originating access service to the actual IXC retail service provider should somehow be responsible for providing terminating compensation to the CMRS provider in the form of reciprocal compensation for the termination of the IXC's retail call. Despite the fact that the IXC is the carrier using the CMRS provider's network for terminating calls, and despite the fact that the Commission has stated that reciprocal compensation applies to local exchange, and not interexchange service, some, but not all, of the CMRS providers continue to confuse this issue with their suggestion that the LEC should be responsible for payment. These CMRS providers seemingly want to burden LECs with payment for compensation to cover the CMRS providers' failure to negotiate proper compensation arrangements with IXCs.[100]

[100] The Rural Alliance supports the ability of CMRS providers to bill and collect from IXCs for IXC calls that terminate to CMRS providers. The dilemma under which CMRS providers cannot collect from IXCs should be corrected immediately.

Accordingly, the Commission should once again confirm explicitly that under existing rules, it is the IXC that is responsible for the payment of terminating charges, and for the payment to the CMRS provider's wireless end user, of all of that IXC's service calls.

4. The Commission Should Affirm its Classification of Dial-Up Traffic Between LECs And ISPs as Exchange Access, and that the ESP/ISP Exemption Applies Only to the Originating Dial-Up Traffic to the ISP. Terminating Traffic from the ISP to the PSTN Must Pay Access Charges.

Confusion and uncertainty regarding the existing interconnection rules can largely be alleviated by the Commission's affirmation to ensure proper implementation of its end-to-end analysis that classifies dial traffic between ISPs and LECs as non-local interstate traffic.[101] The Commission observed that ISP-bound traffic is analogous to long-distance traffic, in particular Feature Group A traffic,[102] because the connection does not generally terminate at the ISP's local server but continues on to distant Internet sites.[103] The originating dial up traffic directed to an ISP is not subject to originating access charges by virtue of the Commission's determination to apply an exemption.[104]

A few parties attempt to utilize the ISP/reciprocal compensation arbitrage problem to bolster support for the discredited mandatory bill and keep proposals for

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[101] *I/M/O Intercarrier Compensation for ISP-Bound Traffic: Order on Remand and Report and Order,* CC Docket No, 99-68, FCC 01-131, 16 FCC Rcd 9151 (2001) ("*ISP Remand Order*").

[102] *ISP Remand Order* at para. 60

[103] *ISP Remand Order* at para. 12. Verizon agrees with the Commission's end-to-end analysis that ISP-bound traffic is interexchange, interstate access traffic and observes that there is no clear distinction between ISP-bound traffic and other forms of traffic that do not terminate locally, including calling card, Feature Group A and switched access traffic generally. *See* Comments of Verizon. Attachment D, at 6.

[104] *See I/M/O MTS and WATS Market Structure: Third Report and Order*, 93 FCC 2d 241 (1983).

intercarrier compensation.[105] Their arguments are both inconsistent with the Commission's end-to-end analysis and are unnecessary. The continued proper classification of ISP-bound traffic fully addresses the issue.[106]

In addition to the affirmation of the Commission's classification of ISP traffic, it is essential that the Commission reject the arguments of those parties that would attempt to avoid the assessment of access charges when IP-enabled telecommunications services are terminated over the PSTN. Some parties suggest that the mere provision of an information service should render a provider exempt from all access charges. This argument fails to recognize that different service applications may be provided by a single provider. A single provider may offer both information services that may be exempt from access charges, and telecommunications services that are not exempt.[107]

The Rural Alliance respectfully urges the Commission to resolve the *WorldCom v. FCC* remand[108] by reaffirming that traffic between LECs and ISPs is exchange access, and that terminating access charges apply to ISP traffic terminated to a LEC through the PSTN.[109]

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[105] *See e.g.* Comments of Qwest at 14, ICF at 26.

[106] Qwest concerns about disruptions inherent in a CPNP structure and about the use of VNXX to service ISPs are addressed. *See* Comments of Qwest at 20 and 44, 45.

[107] *See, e.g.,* Comments of ITTA at 6. ITAA argues that when ISPs are providing e-mail service, for example, the ISP is providing an information service, not a telecommunications service. ITAA ignores the fact that the provision of an information service does not mean that telecommunications is not also being provided. A voice conversation is an application that undoubtedly traverses the network to which access applies when terminated over the PSTN.

[108] *WorldCom v. FCC*, 246 F.3d 690 (DC Cir. 2001).

[109] In this regard, the Rural Alliance is particularly concerned with the continuing wrongful practice of some carriers to claim exemption from access charges by terminating interexchange telecommunications

D. THE IMPLEMENTATION OF A UNIFIED INTERCARRIER COMPENSATION REGIME REQUIRES THE ESTABLISHMENT OF LOCAL RATE BENCHMARKS IN ORDER TO ENSURE THAT A BALANCED SYSTEM OF END USER RATES, INTERCARRIER COMPENSATION, AND UNIVERSAL SERVICE SUPPORT IS MAINTAINED.

The Rural Alliance recognizes that local rate benchmarks are appropriate in order to maintain the public policy goal of comparable local rates in urban and rural areas. [110] The proposals of the Rural Alliance and other parties[111] to implement a unified intercarrier compensation rate require thoughtful review of how best to maintain an appropriate balance of end user rates, intercarrier compensation, and Universal Service support. In response to this need, the Rural Alliance proposed that a composite local exchange end user benchmark rate be established for purposes of rate comparability and to minimize the impact on the Universal Service system. A true measure of comparability is the total composite rate that end user customers pay for similar services.

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transported using Intemet protocol through "local" business lines and other facilities that are not intended for terminating interexchange traffic.

[110] *See* FNPRM at para. 108.

[111] There is widespread support for the adoption of a local service benchmark. JSI describes the benefits of benchmarks "as a vehicle to assist in maintaining revenue neutrality, to assist in leveling out jurisdictional and regulatory concerns, assist in the broadening of the base of possible USF contributors, assist in minimizing the cost impact on both the Federal and state Universal Service support programs and to reinforce equity of Universal Service Fund distributions while at the same time upholding the overall concepts of Universal Service." (JSI at 15) CTA-WTA-OITA observe that in establishing a benchmark rate level, it will also be necessary to provide an efficient methodology for carriers with rates below the benchmark level to get their rates to this level. (CTA-WTA-OITA at 35) Cable provider Cox Communications also supports the local service benchmark concept stating "The Commission should adopt a national benchmark that would include increasing local rates (including SLCs) to avoid adding to the Universal Service burden" (Cox at 13) The value of establishing a local service benchmark is also recognized by consumer groups and state commissions. NASUCA states that "there should be a minimum required level of contribution from local rates before there is recourse to additional Universal Service Funding" (NASUCA at 50). The Missouri PSC states that setting of the benchmark level should be part of a collaborative process, "the Commission selects the plan for unified compensation and then initiates a further proceeding to seek input on such things as determining the appropriate benchmark." (Missouri PSC at 32-34) The South Dakota PUC concurs stating "Another way to minimize the impact [on the Universal

This measure is consistent with the common sense view that the total basic recurring charge for end user customers is the combination of local rates and SLCs. Accordingly, the composite benchmark should include both.[112]

The creation of local exchange benchmark rates affects the states, which bear the responsibility for establishing end user customer rate levels, as well as the Commission, in its overall role of establishing a national framework for intercarrier compensation and Universal Service reform. The Commission should consequently affirm that local exchange benchmark rates will be established and refer the issues of level and implementation to the Joint Board.

IV. THE IMPLEMENTATION OF A UNIFIED INTERCARRIER COMPENSATION REGIME SHOULD NOT ADVERSELY AFFECT OR BURDEN UNIVERSAL SERVICE MECHANISMS.

By any unbiased measurement, the nation's Universal Service policy has been and continues to be a success.[113] As called for by the Universal Service statutes contained in the Act, customers served by the more than 1,200 rural LECs continue to receive services that are affordable and comparable to those services received by customers in urban areas. Congress codified the long-standing Universal Service policy by requiring explicitly that all providers of telecommunications services contribute to Universal Service Funding and that eligible service providers receive specific and predictable

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Service Fund] is to insure that carriers do not recover more from the fund because the carrier has chosen to charge lower rates." (South Dakota PUC at 11)

[112] *See* Comments Rural Alliance at 79.

[113] Universal service can be termed a success not only by measures of consumer access to the PSTN, as virtually all Americans have access to the network, but also by measure of telecommunications subscribership. The FCC's most-recent study reports that 94.2 percent of households have telephone service. *See, Trends in Telecommunications Service*, 2005 Report, Federal Communications Commission, Industry Analysis and Technology Division (rel. Jun. 5, 2005)

funding.[114] The Act defines the services subject to Universal Service and creates a formal process to expand that definition. Customers served by rural LECs are the beneficiaries of the switching, transmission, and transport infrastructure made possible by Universal Service support. This infrastructure allows citizens in even the most rural parts of America to participate actively in and enjoy the benefits of a global economy, and to live and work in rural America without being isolated or disadvantaged.

Although the system's record of success speaks for itself, support is still needed and the policy cannot be discontinued. Stable Universal Service funding remains an ever-vital component of cost recovery and regulated rate design to reimburse carriers for a portion of the investment costs and expenses incurred to provide service to rural customers. Infrastructure investments are not one-time costs, nor are these investments "paid in full" at the point of installation. The cost of maintaining and upgrading the network and paying debt service is ongoing; continued Universal Service support is essential to maintain the existing network and to ensure future investment. The Rural Alliance is committed to working with the Commission to make improvements to the system. The Universal Service system has recently undergone intense scrutiny and, in some instances, criticism. Universal service mechanisms have served this nation and its tens of millions of constituents well, and must be preserved.

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[114] In the Act, Congress acknowledged the national policy of Universal Service and went beyond the previously standing concept of providing access to telecommunications and connecting consumers to one another. The Act states: "… so as to make available, so far as possible to all people of the United States, a rapid, efficient, nation-wide, and world-wide wire and radio communications service with adequate facilities at reasonable charges." As a result, for the first time "Universal Service" included a commitment to making service economically accessible, or affordable, to all Americans. It was not enough that consumers have telecommunications or access available; public policy declared that telephone service prices be affordable for all Americans.

One theme that resonates in the comments of numerous parties is that additional support from the Universal Service Fund (USF) or another mechanism will be necessary to recover revenues lost through reductions in intercarrier compensation rates.[115] Another theme is the desirability of implementing intercarrier compensation reform without unnecessarily large increases in USF,[116] especially since the existing fund is considered by some to already be unsustainably large. A fundamental and troubling inconsistency exists between these two positions: reliance on USF for additional cost recovery while at the same time recognizing that even the existing USF is potentially unsustainable. That inconsistency should lead the Commission to the sound, policy-based conclusion that this proceeding and others should endeavor to ensure a sustainable USF and at the same time remain consistent with statutory requirements for end user rate comparability.

A. A RATIONAL BALANCE OF AFFORDABLE END USER RATES, INTERCARRIER COMPENSATION, AND USF SUPPORT CAN BE MAINTAINED BY ADOPTION OF THE RURAL ALLIANCE PROPOSAL.

Neither the record in this proceeding nor valid public policy support intercarrier compensation changes that would threaten the viability of the Universal Service

[115] *See, e.g.,* Comments of CenturyTel at 37; Cincinnati Bell at 11; Comporium at11; Eastern Rural Telecommunications Association at 2; ICF at 31-33; ICORE at 8; Minnesota Independent Coalition at 27, 29; Mpower Communications at 12; NARUC Proposal Version 7 at 8-12; NASUCA at 11; National Cable Telecommunications Association (NCTA) at 5; National Telephone Cooperative Association (NTCA) at 26; South Dakota Telecommunications Association at 3; SureWest Communications at 30; TDS Telecom at 25; Time Warner Telecom, Convergent, Cbeyond, and Lightship at 5, 6; United States Telecom Association (USTA) at 38; Wisconsin Telecommunications Association at 2; and XO Communications at 20.

[116] *See, e.g.,* Comments of California Telecommunications Association, Oregon Telecommunications Association and Washington Telecommunications Association at 34; Iowa Telecommunications Association at 8; NASUCA at 5-11; Nebraska Public Service Commission at 8-9; New Jersey BPU at 5; Ohio Public Utilities Commission at 23; Qwest Communications at 18; South Dakota PUC at 11; South Dakota Telecommunications Association at 3; SureWest Communications at 33; TCA at 4; and Time Warner Telecom, Convergent, Cebyond and Lightship at 5.

mechanisms by imposing unnecessary increases in the USF and end-user rates. Various measures that would result in comparable end user rates and unified intercarrier compensation rates, while limiting the impact on end user rates and the USF, can be readily accomplished. Consistent with its Comments in this proceeding, the Rural Alliance proposes that the following steps will achieve significant progress toward the Commission goals:

- Set rural LEC intercarrier compensation rates based on embedded costs.

- Impute a nationwide end user rate benchmark, inclusive of both SLCs and local rates, in Universal Service Funding. Such a benchmark will encourage LECs to raise end user rates to the benchmark to ensure that all consumers nationwide are paying reasonably comparable rates.[117]

- Allow LECs to increase Federal SLCs to the current caps as a means of recovering reductions in intercarrier compensation before seeking Universal Service Funding.[118]

- Minimize so-called "phantom" traffic, which is traffic that is wrongly terminated without payment of intercarrier compensation. Carriers that interconnect the traffic of other providers to a LEC should be required to provide billing records with information sufficient to enable the terminating LEC to accurately bill the intercarrier compensation due for the use of its network. In addition, the Commission should implement rules that require all network users to pay for their network use and invoke sanctions for those carriers that abuse these rules.

Individually, each of these steps is consistent with sound public policy and would represent progress toward the Commission's objectives. Collectively, these steps will enable the accomplishment of significant intercarrier compensation reforms while

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[117] Consumers recognize their composite rate as representing both the Subscriber Line Charge (SLC) and their basic local rate. A comparable nationwide benchmark should incorporate both of these rates.

[118] This recommendation recognizes that most price cap carriers' current SLCs are well below the $6.50 and $9.20 caps for residential/single-line business and multi-line business SLCs, respectively.

minimizing the impact on already-strained USF resources, thereby benefiting all customers and carriers on a technologically neutral basis.

B. QUANTITATIVE ANALYSIS OF THE PROPOSALS ON THE RECORD DEMONSTRATES THAT THE RURAL ALLIANCE PROPOSAL IS THE ONLY PROPOSAL THAT PROVIDES A RATIONAL BALANCE OF END USER CHARGES, INTERCARRIER COMPENSATION, AND UNIVERSAL SERVICE FUNDING; THE IMPLEMENTATION OF THE PROPOSALS OF OTHER PARTIES WOULD RESULT IN EXCESSIVE AND UNNECESSARY INCREASES IN END USER RATES AND UNIVERSAL SERVICE FUNDING.

The Rural Alliance has undertaken a quantitative analysis of most intercarrier compensation reform proposals in the record. This analysis reveals that only the recommendations made by the Rural Alliance will minimize the impacts to the USF and end user rates while at the same time achieving the goal of modifying intercarrier compensation appropriately. Other proposals will overburden the USF and unnecessarily increase end user rates and thus undermine and destabilize the very mechanisms (affordable rural end user rates comparable to those in urban areas and sustainable USF support) that Congress and the Commission established to ensure rural customer connectivity to the nationwide telecommunications network at reasonable rate levels.

The model utilized for this analysis – the Rural Alliance Model (RAM) – along with the underlying logic and assumptions is described in Appendix B. The model is populated with the most current publicly available data and the overall results of the model are believed to be as accurate as possible. Nevertheless, the model does not reflect the actual impact that would be experienced by any single company because averages were used to estimate inputs. In order to directly compare the revenue shifts between plans, no demand changes or intermediate transition steps were modeled – only the end state of each plan was modeled. The “end state” financial parameters associated with each proposal are shown below in Table 1.

Table 1 - Intercarrier Compensation Plan Parameters

		Originating	Terminating	Inter Carrier Compensation Rate	SLC Rate	Change in Basic Residential Single Line (R1) Rate	Residual Recovery Mechanism
		-A-	-B-	-C-	-D-	-E-	-F-
1	**ICF**						
	Price Cap	No	No	$ -	$ 10.00	n/a	Yes
	RoR	No	Yes	$ 0.0095	$ 10.00	n/a	Yes
2	**BellSouth**						
	Price Cap	Yes	Yes	Tandem Rate $0.0025	$ 12.00	n/a	No
	RoR	Yes	Yes	End Office Rate $0.00125	No Cap	n/a	No
3	**NASUCA**						
	Price Cap	Yes	Yes	$ 0.0055	No Change	$ 0.12	Limited to $278M
	RoR	Yes	Yes	$ 0.0095	No Change	$ 2.24	Limited to $572M
4	**NARUC v7**	Alternative 1					
	Price Cap	No	$ 0.0010	See Orig&Term	Rates assumed to be at Benchmark (Note 1)		Yes
	RoR	No	$0.0047 blended	See Orig&Term	+$2.63 combined SLC & R1 (Note 1)		Yes
		Alternative 2					
	Price Cap	$ 0.002	$ 0.0010	See Orig&Term	Rates assumed to be at Benchmark (Note 1)		Yes
	RoR	$ 0.002	$0.0047 blended	See Orig&Term	+$2.63 combined SLC & R1 (Note 1)		Yes
5	**CBICC**						
	Price Cap	No	Yes	$ 0.00212	$0.50/Yr until cap	n/a	No
	RoR	No	Yes	$ 0.00212	$0.50/Yr until cap	n/a	Yes
6	**CTIA/Western Wireless**						
	Price Cap	No	No	$ -	No Change	n/a	No
	RoR	No	No	$ -	No Change	n/a	No
7	**Rural Alliance**						
	Price Cap	Yes	Yes	$ 0.0060 *	$7.30	n/a	Yes
	RoR	Yes	Yes	$ 0.0200 *	$7.30	$ 2.67	Yes

* - Average rate used for illustrative purpose. Rate does not represent unified rate for every carrier.

Note 1: In the NARUC plan, after year 3 the permanent rate benckmark will be set to equal 125% of the national average rate. For Rate of Return carriers, we estimate this to be an additional $4.12 per line per month beyond the $2.63 shown in column D/E.

The RAM was used to analyze proposals of the following parties: ICF, BellSouth, NASUCA, NARUC Version 7 and CBICC.[119] In addition, an analysis of the Rural Alliance plan is provided. Table 2 below shows results of the RAM analysis.

[119] The CTIA and Western Wireless plans were not modeled, as they are essentially "bill and keep" plans with all existing intercarrier revenues being absorbed by the end user. An analysis of the Qwest plan was not included because the plan's parameters did not fit within the capabilities of the RAM. Parties that advocated broad principles, but provided no numeric data, were not modeled.

Table 2 - Intercarrier Compensation Results ($ in Millions)

			Inter Carrier Compensation Revenue	Additional SLC Revenue	Basic Residential Single Line (R1) Revenue	Residual	Recovery Mechanism	Residual not addressed in Plan
			-A-	-B-	-C-	D=A+B+C	-E-	-F-
1	**ICF**							
		Price Cap	$ (6,287)	$ 6,700	$ -	$ -	$ -	$ -
		RoR	(2,475)	521	0	(1,954)	1,954	0
		Total	$ (8,762)	$ 7,221	$ -	$ (1,954)	$ 1,954	$ -
2	**BellSouth**							
		Price Cap	$ (4,544)	$ 9,972	$ -	$ -	$ -	$ -
		RoR	(2,988)	2,988	0	0	0	0
		Total	$ (7,532)	$ 12,960	$ -	$ -	$ -	$ -
3	**NASUCA**							
		Price Cap	$ (2,451)	$ -	$ 196	$ (2,255)	$ 278	$ (1,977)
		RoR	(2,475)	0	266	(2,209)	572	$ (1,637)
		Total	$ (4,926)	$ -	$ 462	$ (4,464)	$ 850	$ (3,614)
4	**NARUC v7**							
	Alternative #1							
		Price Cap	$ (5,590)	$ -	$ -	$ (5,590)	Note 1	$ (5,590)
		RoR	(2,857)	0	312	(2,545)	Note 1	(2,545)
		Total	$ (8,447)	$ -	$ 312	$ (8,135)		$ (8,135)
	Alternative #2							
		Price Cap	$ (5,241)	$ -	$ -	$ (5,241)	Note 1	$ (5,241)
		RoR	(2,773)	0	312	(2,461)	Note 1	(2,461)
		Total	$ (8,014)	$ -	$ 312	$ (7,702)		$ (7,702)
5	**CBICC**							
		Price Cap	$ (4,808)	$ 1,643	$ -	$ (3,165)	Note 1	$ (3,165)
		RoR	(2,933)	157	0	(2,776)	Note 1	(2,776)
		Total	$ (7,741)	$ 1,800	$ -	$ (5,941)		$ (5,941)
6	**CTIA / Western Wless**							
		Price Cap	$ (6,287)	$ -	$ -	$ (6,287)	Note 1	$ (6,287)
		RoR	(3,066)	0	0	(3,066)	Note 1	(3,066)
		Total	$ (9,353)	$ -	$ -	$ (9,353)		$ (9,353)
7	**Rural Alliance**							
		Price Cap	$ (2,103)	$ 2,281	$ -	$ -	$ -	$ -
		RoR	(1,822)	99	317	(1,406)	1,406	0
		Total	$ (3,925)	$ 2,380	$ 317	$ (1,406)	$ 1,406	$ -

Note 1 - Revenue Replacement Mechanism Amount Undefined.

As Table 2 illustrates clearly, the Rural Alliance plan produces a reasonable balance between intercarrier compensation rate changes and end user rate increases without creating unreasonable increases to explicit funding mechanisms and end user rates. All other plans generate SLC increases, create an unsustainable residual requirement, or leave companies with a revenue shortfall. Following are summaries of the Rural Alliance's assessment of various plans based on the RAM analysis:

1. ICF—The RAM analysis of the ICF plan shows no additional support is required for the price cap carriers and $1.95 billion in support is required for the rural LECs. This amount compares to the approximately $2.1 billion calculated by ICF for Step 5 of its plan.[120] While there is a difference in the additional support created for the rural LECs, this variation is likely a result of the base intercarrier revenues assumed in the two models.[121] Regardless of the model assumptions, the ICF plan places a disproportionate share of additional funding on an already vulnerable Universal Service Funding and allows end user SLC rates for some customers to increase significantly. In addition, even if price cap LECs were to forego SLC increases to the new caps, these LECs still fare exceedingly well under the ICF plan because of the transiting revenue opportunities the plan creates and the reciprocal compensation expense decreases.

2. BellSouth—The Bell South plan with a rural LEC intercarrier rate even lower than the ICF plan, creates an even larger residual funding requirement. The BellSouth plan, with an uncapped SLC for rural LECs, would require an average SLC increase of slightly over $19.00 per month (for an SLC that approaches, on average, $26.00) to recover completely the shortfall. By contrast, the price cap LECs gain revenue if they increase the average SLC by roughly $6.00 per line per month to a $12.00 cap and charge "transiting" charges at twice the end office rate. These price cap revenue gains do not include the reciprocal compensation expense decreases that these companies would also experience.

3. NASUCA—Under the NASUCA plan, the residual revenue calculated by the RAM as a result of intercarrier rate changes is $4.46 billion, as compared to a $3 billion residual calculated by NASUCA.[122] Since the NASUCA plan constrains additional funding to $850 million, the Rural Alliance analysis estimates a remaining revenue shortfall of $3.6 billion, which equates to $10.48 per line per month for the average rural LEC customer and $1.21 per line per month for the average price cap customer. Recovering this

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[120] *See* Comments of ICF ,Appendix B, B-14.

[121] As further described in Appendix B, there is no publicly available source for intrastate access revenues. This necessitates the development of estimates for these revenues. Thus, to the extent that different models make different assumptions in the estimation of intrastate revenues, their outputs will vary accordingly.

[122] *See* Comments of NASUCA at 21.

shortfall from end user customers would be at odds with the affordable, just and reasonable and urban rate comparability requirements of the Act.

4. NARUC Version 7—The NARUC Version 7 plan creates a residual of between $7.7 and $8.1 billion, depending on whether an originating rate is included or not. The large residual is a result of the low intercarrier rates selected for price cap LECs and rural LECs alike. When expressed on a per-line basis, rural LECs have a residual almost five times larger than price cap carriers that would need to be recovered from end users. As with the NASUCA plan, recovering this shortfall from end user customers would be at odds with the affordable, just and reasonable and urban versus rural rate comparability requirements of the Act.

5. CBICC—The CBICC plan's virtually non-existent intercarrier compensation terminating rate produces a $5.9 billion residual, with 45 percent of that attributed to the rural LECs. Aside from the end user charge increases, the CBICC plan does not provide any additional funding for price cap LECs. Replacement funding for rural LECs is unclear under the plan. Again, if the residual is recovered from the end users of the LECs, the result would be at odds with the affordable, just, and reasonable and urban versus rural rate comparability requirements of the Act.

6. CTIA and Western Wireless—The CTIA and Western Wireless plans are "bill and keep" plans; thus, the entire ILEC access revenue stream of $9.3 billion must be recovered from other sources. If the shortfall were recovered entirely from end users, then local rates would need to increase an average of $3.84 per line per month for customers of price cap LECs and an average of $19.62 per line per month for customers of rural LECs. For many rural LECs, the customer impact would be much higher than the average.

7. Rural Alliance— By applying an average $0.02 per minute intercarrier compensation rate[123] for rural LECs, a $2.67 residential end user increase for rural LECs, and a SLC increase to the current caps for all carriers creates a residual of $1.4 billion. There would be no residual for price cap LECs if price cap carriers raised their SLCs to the current caps and billed a $.006 per minute intercarrier compensation rate.

The basic conclusion that can be reached from this analysis is that only the Rural Alliance plan results in a balanced and fair reform of the intercarrier compensation

[123] This rate reflects a reasonable estimate of the average of the unified rates for rate-of-return companies that the Rural Alliance believes would result from the rate-setting methodologies recommended two rural Alliance sponsor groups, the ARIC and EPG.

system while at the same time addressing comparable end user rates and minimizing the impact on the USF.

C. THE RURAL ALLIANCE ANALYSIS DEMONSTRATES THAT A BALANCED APPROACH WILL ADDRESS INTERCARRIER COMPENSATION PROBLEMS AND MINIMIZE USF IMPACTS.

The analysis facilitated by the RAM provides reasonable, best-available data to demonstrate that the balanced approach proposed by the Rural Alliance will positively address the problems with intercarrier compensation, result in comparable rates, and minimize effects on USF. An overarching result that the RAM data show is that the huge market-size disparity between price cap and rate-of-return companies requires that any changes must be put in proper perspective in assessing the overall results of all proposals. That being the case, several conclusions can be ascertained from the RAM analysis:

- Many of the plans that essentially eliminate intercarrier compensation rates would increase significantly both end user rates (through SLC increases) and the USF. These proposed changes that would have a detrimental impact on both end users and the sustainability of the USF are unnecessary if reasonable and embedded cost-based intercarrier compensation rates (both originating and terminating) are maintained for rural LECs.
- Since rural LECs constitute fewer than 10 percent of the nation's overall access lines, changes to rural LECs' local, SLC, or intercarrier compensation rates do not have a significant overall impact when compared to the overwhelming size of the price cap market. For example, a \$.01 per-minute change in the average rural LEC intercarrier

rate represents $621 million that has to be otherwise recovered, while the same $.01 per-minute change in price cap rates equals $6.9 billion.

- Since rural LECs constitute fewer than 10% of the nation's overall access lines, changing rural LECs' local rates to a benchmark rate that is equal to the average urban rate will recover only a small fraction of the intercarrier compensation reductions.
- Price cap carriers have so many access lines that even small changes in end user rates can recover significant decreases in intercarrier compensation rates. An average rate increase of $3.84 per line would absorb all intercarrier compensation revenues, and this does not account for transiting revenues or expense savings that price cap carriers would likely experience.
- If both price cap carriers and rural LECs were to move to bill and keep without any other changes, and both were to recover the lost revenues from USF, 67 percent of the USF would go to price cap carriers, even though their rates decreased, on average, $0.009 per minute. By comparison, 33 percent of USF would go to rural LECs, even through on average their rates decreased $0.049 per minute.[124]
- Plans that only allow a terminating rate to be charged have almost double the impact on USF or other residual funding.
- Under the ICF plan, end user rates will increase approximately three times more than the end user rate increases proposed by the Rural Alliance, and under the BellSouth plan, they would increase by more than five times.

[124] CLECs are not included in this example. If they are included, the RAM produces this USF distribution: price caps, 58 percent; rate of return carriers, 28 percent CLECs, 14 percent.

- The combination of increased transiting revenues, expense savings resulting from reduced reciprocal compensation payments and SLC increases could result in price cap carriers increasing their *net* overall revenues, as is demonstrated in the BellSouth plan.
- If the identical-support rule stays in place, the "multiplier effect" caused by multiple eligible telecommunications carriers (ETCs) being designated in certain study areas will cause the overall USF impact to greatly exceed that identified by the RAM. The RAM only shows the initial impact of moving revenue recovery to USF or another residual mechanism. As additional ETCs are designed, more USF would be required.
- The results show average effects across carriers. An individual LEC's impact can differ greatly from the average.

D. THE ICF PLAN RESULTS IN EXCESSIVE INCREASES IN END USER RATES AND USF SUPPORT THAT MAY BE AVOIDED.

The ICF plan, by the end of its implementation phases, would result in approximately an $8.7 billion shortfall with more than $7 billion recovered from end users and almost $2 recovered from additional Universal Service support, much of it resulting in support flowing to rural companies.[125] There is cause for concern that increases in USF would lead to additional claims about the future of the USF system, which some already believe is in a crisis due to its growth. The Commission should be concerned about the significant end user rate increases under this plan, as well. The Rural Alliance recommendations, however, along with an accurate accounting for other

[125] The Rural Alliance RAM analysis of the ICF plan, as discussed earlier, produces a larger residual funding requirement for Rural LECs than ICF estimates but no residual for price-cap LECs.

opportunities for price cap companies that ICF does not quantify, enable a greatly minimized impact on end user rates and the USF.

1. The ICF Plan Increases Inordinately the Dependency of Rate-Of-Return LECs on Universal Service as a Result of the ICF's Failure to Balance a Rational Level of Intercarrier Compensation With End User Rates and Universal Service Funding.

Of the $2.744 billion in additional USF requirements the ICF predicts its plan would create, more than $1.6 billion of that amount would go to rural LECs.[126] This means rural LECs would account for almost 60 percent of the USF that the plan claims to create.[127] Of course, rural LECs' total intercarrier compensation revenues are far less than those of the price cap carriers. The ICF model reports that non-rural switched access revenues that are shifted under the plan would total almost $7.3 billion,[128] while rural LEC access revenues total about $2.4 billion.[129] Assuming the ICF data are accurate, rural LECs would account for less than *one-third* of the overall access revenues, yet would receive almost *two-thirds* of the total new USF that would result from the ICF plan. This skewed result shows that sustainability of USF is especially critical to rural LECs and their customers.

Under the ICF plan, the goals of Universal Service, minimizing the impact on USF and providing comparable end user rates, is not accomplished. Rather, the plan

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[126] *See* Comments of ICF, Appendix B (ICF Model Documentation), at B-14.

[127] The ICF model makes no attempt to quantify the amount of portable support to other Eligible Telecommunications Carriers that would result from its plan, which would further increase the impact on USF.

[128] *Id*. at B-20.

[129] *Id.* at B-21.

evinces a goal to create a disproportionate growth in USF for rural LECs.[130] As the Rural Alliance has demonstrated in its above analysis, minimal impacts on USF could be achieved if modest intercarrier compensation rates were established and SLC increases to current caps were implemented or imputed. Minimizing the impact on the USF and end user rates should be a policy objective of all parties, but the ICF plan as presented would not produce such a result for rural LECs and the customers they serve. Additional USF should only be the last cost-recovery option in order to not imperil a system that is being politically targeted because of its previous growth, most of which has been predictable given Commission policies and the congressional direction to make all support explicit.

2. The ICF Proposal for Permissive Subscriber Line Charge Increases in Combination with the Discontinuation of Price Cap Regulation is Unnecessary.

The ICF plan would increase SLC caps for both price cap and rural companies over a series of years to an ultimate cap of $10 for both residential/single-line business and multi-line business customers (renamed Mass Market and Enterprise customers, respectively, in the plan).[131] However, effective July 1, 2008, or the start of Year 4 of the plan, price cap regulation would be discontinued, allowing these companies to price SLCs as they wish.[132]

Based on its analysis, the Rural Alliance finds that the increased SLC caps in the ICF plan are unnecessary as a means of recovering most intercarrier compensation

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[130] *See* Comments of ICF at 34.

[131] *See* Comments of ICF, Appendix D, Sections III.G. and H.

[132] *Id.*, at III.J.2. (p. 68).

revenues for price cap LECs. This is because price cap LECs can recover most of these revenues under the existing SLC caps. Therefore, increasing the caps as ICF proposes would only exacerbate rate comparability problems between urban and rural customers, since rural LECs would need to increase SLCs in order to recover their intercarrier compensation reductions. The ICF plan's SLC proposal is unnecessary and counterproductive to maintain comparability.

3. The Economic Benefits of the ICF Proposal to Larger LECs is Even More Significant Than the ICF Indicates. The ICF Has Failed to Quantify Both the Terminating Expense Savings and the "Transit" Revenues That Will Benefit Large Carriers.

Through its implementation of bill and keep for most intercarrier compensation, the ICF plan would relieve many LECs of the large reciprocal compensation obligations they have experienced with CLECs that serve dial-up Internet Service Providers (ISPs).[133] While RBOCs and other price cap LECs would experience substantial reciprocal compensation expense reductions under the ICF plan, neither the group's comments nor its model attempt to quantify these financial benefits. Such expense reductions would flow immediately to the companies' bottom lines, and this should be taken into account in determining the net effects of this or any plan.

In addition to these unaccounted-for expense savings, the ICF plan also provides for continuation of intercarrier compensation opportunities for companies that operate tandem switches. RBOCs and other price cap companies are the primary tandem operators today, and thus would be the beneficiaries of these monopoly rents and is further evidence of the market power that these carriers possess. The ICF establishes

[133] *See* Comments of ICF, Appendix D, at Section III.E.

rates and terms for "tandem transit service," which includes tandem switching and tandem switched transport[134] that are currently provided in exchange access and reciprocal compensation arrangements. The ICF plan maintains existing intercarrier revenue opportunities and creates new ones for transiting providers, since under the plan any traffic that originates on one network and terminates on another while utilizing the tandem switching and transport of a third carrier would create a compensation obligation.

Given that price cap companies would derive both reciprocal compensation expense savings and the transiting revenues under the ICF plan, it is critical that these benefits be accounted for in the checks and balances that are made in assessing that plan. The ICF plan, as modeled by that group, produces substantial USF requirements and raises SLCs for rural LECs, but does not account for transiting revenues and expense savings that will occur for price cap LECs.

E. PARTIES THAT PROMOTE EXCESSIVE CHANGES TO INCREASE RURAL CARRIER DEPENDENCY ON UNIVERSAL SERVICE FUNDING ARE SUPPORTING EFFORTS OUTSIDE OF THIS PROCEEDING TO DESTABILIZE THE UNIVERSAL SERVICE NETWORK SUPPORT SYSTEM.

The ICF claims that its plan addresses the "special concerns" of rural consumers with steps that stabilize rural markets, facilitate services reasonably comparable to urban areas, and preserve and enhance Universal Service.[135] The Rural Alliance respectfully disagrees.

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[134] *Id.* at 26.

[135] *See* Comments of ICF at 34.

At first blush, the ICF's public statements espousing concern for the future of Universal Service may appear genuine. The ICF comments in this proceeding proclaim that a "true commitment to Universal Service requires a long-term, stable funding source."[136] Upon closer examination, however, it is apparent that such proclamations are not supported by the collective indirect actions of the RBOCs and other large companies. The public policy efforts these companies are co-sponsoring seek to undo the very Universal Service Fund into which the ICF plan would funnel billions of additional dollars in revenues. While plans like that of the ICF would significantly and unnecessarily increase end user rates and significantly increase the current USF to recover costs now part of intercarrier compensation, the four RBOCs are members of a "think tank" and a "coalition" that are at the forefront of attacks on the existing USF system.[137]

The Progress and Freedom Foundation (PFF) was founded in 1993 to, along with other missions, advocate what it says is "market-oriented policy" in telecommunications and media.[138] This foundation has directly called for eliminating USF support for carriers,[139] which is at odds with the position certain of the PPF supporters are taking in

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[136] *See* Comments of ICF at 17, 31.

[137] *See* www.pff.org/about/supporters.html and www.teleconsensus.com/portal/members/default

[138] *See* www.pff.org/about/index.html.

[139] In a January 2005 white paper, PFF states that "[i]n our view, to the extent policymakers determine that subsidies for telephone service should be continued," USF should be restructured to provide "special needs subsidies" for households rather than "general subsidies" made available to carriers. *See* "The Myths and Realities of Universal Service: Revisiting the Justification for the Current Subsidy Structure," at p. viii. Available at www.pff.org/issues-pubs/books/050118usfreport.html.

this proceeding, where they recommend maintaining existing USF and substantially increasing USF support for rural LECs.

Meanwhile, a "coalition" called TeleCONSENSUS was launched in April 2005 by the United States Chamber of Commerce to urge Congress to "update" telecommunications laws,[140] substituting market forces for regulation. TeleCONSENSUS lists as members all of the RBOCs.[141] TeleCONSENSUS further believes in "distributing Universal Service Funds via consumer vouchers, not with payments to telephone companies, to allow competition among suppliers and choice for consumers."[142] Here again, the conclusions are directly at odds with the ICF recommendation for expanding the USF.

The Rural Alliance disagrees in the strongest terms possible with the conclusions issued thus far by both groups, and urges the Commission to refrain from adopting a plan such as the ICF proposes that would increase inappropriately the size of the USF for rural LECs.

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[140] *See* TeleCONSENSUS press release. Available at www.teleconsensus.com/press/releases/2005/april/05-58.htm.

[141] www.teleconsensus.com/portal/teleconsensus/members/default.

[142] *See* Summary of Findings, "Sending the Right Signals: Promoting Competition Through Telecommunications Reform," at p. 13. Available at www.teleconsensus.com/portal/teleconsensus/about/default.

V. THE IMPLEMENTATION OF A SUSTAINABLE UNIFIED INTERCARRIER COMPENSATION PLAN SHOULD ENSURE FAIR AND EQUITABLE ACCESS TO THE TRANSPORT SERVICE NECESSARY TO CONNECT RURAL NETWORKS AND THEIR CUSTOMERS TO THE INTERNET.

The Rural Alliance in its Comments recommended that IP interconnection be part of this intercarrier compensation inquiry.[143] The economics of interconnection in circuit-switched and packet-switched networks are essentially the same even though the end-market products and industry structures may differ.[144] The Rural Alliance supports the recommendations that urge the Commission to authorize the SBC/ATT and Verizon/MCI mergers only if merger conditions limit anti-competitive interconnection by the merged entities.[145] The prospect of a single entity that controls a large share of the retail IP and PSTN market *and* owns the transmission assets (either Tier I backbone or interexchange transport) raises the specter of market control not experienced since the divestiture of AT&T.

A number of large companies, and the organization that represents these companies, are advocating commercial agreements as a means to establish interconnection. These entities assert that market-driven commercial agreements are preferable to regulation and will result in innovation, efficiency, lower prices and high-

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[143] *See* Comments of the Rural Alliance at 154.

[144] *See* Comments of the Rural Alliance at 167.

[145] *See, generally, Application for Consent to Transfer of Control filed by SBC Communications, Inc. and AT&T Corp.: Comments of the Independent Alliance*, WC Docket No. 05-65, and *Applications of MCI, Inc. Transferror, and Verizon Communications, Inc., Transferee: Application for Transfers of Control: Comments of the Independent Alliance*, WC Docket No. 05-75, DA 05-762.

quality services.[146] In a commercially negotiated environment, terms are based on negotiation power of the entities involved. It is no surprise that the entities possessing market power want to negotiate commercial agreements, while entities lacking market power request regulatory temperance.

A wide variety of parties that commented on the merger petitions have concerns that parallel those of the Rural Alliance. These concerns include service degradation, price gouging, and refusal to interconnect — both for local and IP backbone facilities. Cox Communications, Inc. notes that "the merged company would have an increased capability and incentive to raise or maintain its transit rates at supra-competitive levels or engage in other anti-competitive conduct."[147] Moreover, "the merged company can impose higher costs on critical inputs, refuse to provide or discriminate in the provision of IP backbone access" according to a group of CLECs.[148] Other parties recognize the interplay between simultaneously being a wholesale and retail provider. The Consumer's Union commented that "SBC and Verizon would have an incentive to abuse their control over those assets to diminish competition for their retail businesses, rather than maximize

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[146] *See* Comments of USTA at 5.

[147] *See I/M/O Verizon Communications Inc. and MCI, Inc. Applications for Consent to Transfer of Control*: *Comments of Cox Communications, Inc.,* WC Docket No. 05-75, at 13.

[148] *See I/M/O Application for Consent to Transfer Control Filed By Verizon Communications Inc. and MCI, Inc.: Comments of ACN Communications Services, Inc., ATX Communications, Inc., Biddeford Internet Corporation d/b/a Great Work Internet, Bridgecom Internation, Inc., Broadview Networks, Inc., Bullseye Telecom, Inc., Cavalier Telephone Mid-atlantic, LLC, Cimco Communications, Inc., CTC Communications Corp, Gillette Global Network, Inc. d/b/a Eureka Networks, Granite Telecommunications, LLC, Lightship Communications, LLC, Lightwave Communications, LLC, Lightyear Network Solutions, LLC, Mpower Communications Corp, Pac-West Telecom, Inc., RCN Telecom Service Inc., U. S. LEC Corp., U.S. Telepacific Corp. d/b/a Telepacific Communications,* WC Docket No. 05-75, at 55.

the revenue flowing over those assets."[149] Similarly, the New York Attorney General stated, "Those Tier 1 providers in control would have both the ability and incentive to, for example, charge significantly higher fees, prioritize their own data packets, block certain ISP transmissions, or end entirely their cooperative relationships with smaller backbones."[150]

The Rural Alliance agrees with Vonage that the Internet market needs to be reexamined now that there are fewer providers of backbone services, barriers to entry are higher, and the market is being concentrated in the hands of local providers who can themselves deny access to local facilities.[151] CLECs, consumer advocates, state regulators, independent ISPs, and VoIP providers issued comments that are in agreement with the recommendations presented by the Rural Alliance: limited regulation to ensure that open, affordable interconnection exists in the IP world. Toward that end, the Rural Alliance recommends that the Commission adopt and implement a set of competitively-neutral interconnection principles, which should include the following:

1. Interconnection should not be a source of competitive advantage.
2. Agreements should be subject to public review.
3. Rates should be cost-based.
4. Companies should not be permitted to refuse interconnection.
5. Compensation should be technology independent.
6. Interconnection provisions should accommodate various sizes of entities.
7. Providers should not discriminate in terms of protocols provided.

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149 *See I/M/O Verizon Communication Inc. and MCI Inc. Applications for Approval of Transfer of Control*: *Petition to Deny of Consumer Federation of America, Consumers Union, and U.S. Public Interest Research Group*, WT Docket No. 05-75, at 24.

150 *See I/M/O Verizon Communications, Inc. and MCI, Inc. Applications for Approval of Transfer of Control: Comments of Eliot Spitzer Attorney General of the State of New York*, WC Docket No. 05-75, at 15.

151 *See I/M/O Application for Consent to Transfer Control Filed by Verizon Communications Inc. and MCI, Inc.: Comments of Vonage Holdings Corp..*, WC Docket No. 05-75, at 8.

The above list should not be considered all inclusive, but rather should serve as a starting point for a further Commission investigation of IP interconnection as recommended by the Rural Alliance in its Comments. As circuit switching is replaced with packet switching, eventually most, if not all, communications will be IP-based. The Commission and the industry owe it to customers to ensure that the market operates in a fair and non-discriminatory manner.

VI. IMPLEMENTATION OF A UNIFIED INTERCARRIER COMPENSATION REGIME REQUIRES A COLLABORATION OF FEDERAL AND STATE REGULATORS TOGETHER WITH COMMISSION ACTION THAT AFFIRMS AND CLARIFIES THE EXISTING INTERCONNECTION RULES.

A. FCC PREEMPTION IS OPPOSED BY A MAJORITY OF COMMENTING PARTIES; THE MOST EXPEDIENT PROCESS TO IMPLEMENT UNIFIED INTERCARRIER COMPENSATION IS A COLLABORATIVE FEDERAL-STATE JOINT BOARD PROCESS.

Some parties to these proceedings suggest that the Commission has the authority to preempt the states' jurisdiction over intrastate access charges and reciprocal compensation arrangements. As the Rural Alliance and many other parties have demonstrated,[152] the plain language of the Act establishes clearly the states' authority in these areas, and presents absolutely no opportunity for Federal preemption of that authority in the absence of Congressional action.

The ICF, for example, argues that the Commission's authority to promulgate rules under Section 251(b)(5) extends to all "telecommunications" involving a LEC, and,

[152] *See, e.g.*, Comments of the Rural Alliance at 139-156; NARUC at 4-14; Public Utilities Commission of Ohio at 2-12; Maine Public Utilities Commission and the Vermont Public Service Board at 4-12.

accordingly, establishes the specific statutory authorization for the Commission to preempt the states' intrastate ratemaking authority.[153] This interpretation is simply incorrect. In both scope and context, the application of Section 251(b)(5) is confined to competitive local exchange interconnection arrangements.[154]

The ICF does not explain how its interpretation of this section of the Act can be read to correspond with the clear jurisdictional boundaries established by Section 152(b) of the Act, which provides that

> *nothing in this chapter* shall be construed to apply or to give the Commission jurisdiction with respect to (1) charges, classifications, practices, services, facilities, or regulations for or in connection with intrastate communication service by wire or radio of any carrier . . . .[155]

Inasmuch as Section 152(b)(1) was not among the many sections of the Act amended or otherwise modified by Congress in 1996, its basic limitations remain intact.[156] Accordingly, even if the ICF were correct in its suggestion that all aspects of "telecommunications" are included within the meaning of Section 251(b)(5), which it is not, the only "telecommunications" which could be included in that definition are those telecommunications which are subject to the Commission's statutory grant of jurisdiction – those which are interstate in nature.[157]

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[153] *See generally*, Comments of the ICF at 37-44 and Appendix A.

[154] *See* Comments of the Rural Alliance at 144-146. *See also,* Comments of Verizon at 34: "What is certain is that the Commission should reject arguments by some parties that it can regulate intercarrier compensation for all traffic through 47 U.S.C. § 251(b)(5)." *See also* Maine and Vermont Comments at 7-9.

[155] 47 U.S.C. § 152(b) (emphasis added).

[156] Pub.L. 104-104, Title VI, § 601(c)(1), codified as note following 47 USC § 152 (1996) ("This Act [Telecommunications Act of 1996] and the amendments made by this Act shall not be construed to modify, impair, or supersede Federal, state or local law unless expressly so provided in such Act or amendments.")

[157] *See generally*, Comments of Maine and Vermont at 5-6.

Some parties argue that the "inseparability" of intrastate and interstate elements of telecommunications provides a basis for preemption of state rule-making authority.[158] This argument fails on factual grounds. The record in this proceeding reflects a long history of identifying and classifying telecommunications traffic by jurisdiction,[159]

Many of those searching for the prize of preemption authority fashion the provisions of Section 251(g) as the keys to the vault.[160] Neither the express language of this section, nor its history or context, suggest that it constitutes authorization of any kind, let alone preemptive jurisdiction over state access charges.[161]

Some parties[162] also suggest that preemption authority is found in Section 201(b) of the Act, which empowers the Commission to "prescribe such rules and regulations as may be necessary in the public interest to carry out the provisions of this Act." This argument fails, however, because Section 201(b) is applicable only where an independent source of statutory authority to act exists. As the Rural Alliance notes herein, the record demonstrates that there is no "provision of this Act" which underlies the Commission's exercise of intrastate rulemaking authority.[163]

The Commission does not possess the authority to preempt intrastate ratemaking. The Rural Alliance submits that no single statutory provision, nor any selection of

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[158] *See, e.g.,* Comments of Verizon at 37-38; USTA at 26-29.

[159] *See, e.g.,* Comments of Rural Alliance at 151-153; Maine and Vermont at 12.

[160] *See* Comments of BellSouth at 43, 44.

[161] *See* Comments of Rural Alliance at 146-149; Maine and Vermont at 10, 11.

[162] *See* Comments of USTA at 25, 26.

statutory provisions, provides the necessary basis to sustain the Commission's authority to preempt state ratemaking jurisdiction. If such authority does exist, there is no agreement even among its proponents as to its source. One truth, however, does emerge from the record in this proceeding: tortuous litigation will nearly certainly ensue from the Commission's assertion of preemptive rights to establish intrastate rates.

It is clear that cooperative Federal-State action is the simplest and most productive avenue to the development and implementation of a sustainable version of a unified intercarrier compensation plan. The Commission and the states are each assigned crucial and complementary roles in resolving the current uncertainties that threaten to undermine the stability of service provision critical to national commerce and public safety, including ensuring the preservation of Universal Service programs. Prudence and rationality join the demands of statutory design in guiding the Commission toward adoption of a joint and cooperative Federal-State approach.

B. THE RURAL ALLIANCE RECOMMENDATIONS PROVIDE A SUBSTANTIVE PROPOSAL AND RATIONAL PROCESS TO IMPLEMENT UNIFIED INTERCARRIER COMPENSATION IN A MANNER THAT WILL SUSTAIN AND ADVANCE THE PROVISION OF UNIVERSAL SERVICE.

Given the complex nature of the intercarrier compensation reform process, and the need to design a transition process that recognizes multiple public interest impacts, it is unreasonable to expect that a single Order issued at the end of this Notice proceeding fully resolving all issues is either possible or desirable. The Rural Alliance respectfully suggests, however that it is possible to utilize this proceeding to define goals and establish an overall framework for intercarrier compensation reform, as well as

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[163] *See* Comments of Maine and Vermont at 6, 7, arguing that no independent authority exists under Section

addressing other issues that can be decided in the near term that would set the stage for further reform. As described in the preceding section the Rural Alliance believes that the only way in which the many complex issues in this proceeding can be implemented is through a collaborative Federal-State effort.

Appendix C to these Reply Comments is a matrix that describes, in detail, a plan to quickly resolve intercarrier compensation issues that can be decided in the near term, and a process to resolve the remaining longer term issues related to establishing and implementing a unified intercarrier compensation regime. It shows the respective roles of the Commission, the Universal Service and Separations Joint Boards (collectively called the "Super Joint Board"), as well as the state commissions. This plan proposes an initial FCC Order to be issued by December 31, 2005 that would address three areas:

1. Reforms that can be implemented quickly;
2. An overall framework for reform and recommendations for the Joint Boards to consider; and
3. Longer term issues, including an FNPRM to consider and optional capacity-based plan for intercarrier compensation.

The next step in the plan would charge the Joint Boards with considering the various issues referred in the FCC Order and issuing Recommended Decisions by September 30, 2006. Based upon these recommendations, the FCC would issue an Order by June 30, 2007 establishing the specific details for the establishment and phase-in of the unified intercarrier compensation rate structure. The first phase of the implementation of the new regime would occur on December 31, 2008, with annual implementation of subsequent

251(b)(5).

phases until the end of the transition process as recommended by the Joint Boards and approved by the FCC.

The specific details of this plan and transition process are more fully described in Appendix C. The Rural Alliance looks forward to continuing to work with the Commission, the Joint Boards, and the various state commissions as this implementation process unfolds.

Respectfully submitted,

THE RURAL ALLIANCE

By: /s/Stephen G. Kraskin

Stephen G. Kraskin
Joshua H. Seidemann
Kraskin, Moorman & Cosson LLC
2120 L Street N.W. Suite 520
Washington, D. C. 20037
(202) 296-8890
skraskin@Independent-tel.com

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